RENEWAL ANNUAL INFORMATION FORM

FOR THE YEAR ENDED DECEMBER 31, 2008

March 31, 2009

HYDRO ONE INC.

ANNUAL INFORMATION FORM
FOR THE YEAR ENDED DECEMBER 31, 2008

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Except where otherwise indicated, all information presented herein is as at December 31, 2008.

DEFINITIONS

For convenience, in this Annual Information Form:

"**CDM**" means conservation and demand management;

"**GTA**" means the Greater Toronto Area;

"**Hydro One**", "**our company**", "**we**", "**us**", and "**our**" refer to Hydro One Inc. and its subsidiaries and predecessors, except where the context requires otherwise;

"**IESO**" refers to the Independent Electricity System Operator, previously named the Independent Electricity Market Operator;

"**IPSP**" means the Integrated Power System Plan developed by the OPA;

"**LDC**" means local distribution company;

"**Market Rules**" means the rules made under Section 32 of the *Electricity Act, 1998* that are administered by the IESO;

"NERC" means the North American Electric Reliability Corporation;

"**OEB**" refers to the Ontario Energy Board;

"**OEFC**" means the Ontario Electricity Financial Corporation;

"**OGCC**" means Hydro One's Ontario Grid Control Centre located north of Toronto, Ontario;

"**Ontario**" refers to the Province of Ontario as a geographical area;

"**OPA**" refers to the Ontario Power Authority;

"OPG" refers to Ontario Power Generation Inc.;

"**Open Access**" refers to the opening of Ontario's wholesale and retail electricity markets to competition which officially occurred on May 1, 2002;

"**Province**" refers to the Government of the Province of Ontario; and

"TS" refers to a transformer station.

CORPORATE STRUCTURE

Hydro One Inc. was incorporated as Ontario Hydro Services Company Inc. by Articles of Incorporation dated December 1, 1998 under the *Business Corporations Act* (Ontario). On May 1, 2000, we changed our name to Hydro One Inc.

Our registered office and head office is located at 483 Bay Street, 15th Floor, North Tower, Toronto, Ontario, M5G 2P5.

The following are our principal subsidiaries, each of which is wholly-owned by us and is incorporated under the laws of Ontario:

- Hydro One Networks Inc. — carries on all business relating to our ownership, operation and management of electricity transmission and distribution systems and facilities;
- Hydro One Brampton Networks Inc. — carries on the business relating to our ownership, operation and management of electricity distribution systems and facilities in Brampton, Ontario;
- Hydro One Remote Communities Inc. — carries on all business relating to our ownership, operation, maintenance and construction of generation and distribution assets used in the supply of electricity to remote communities throughout Northern Ontario; and
- Hydro One Telecom Inc. — carries on all of our business relating to leasing dark fibre and providing lit telecommunications capacity to other telecommunication carriers, large corporations, government, healthcare, and education institutions.

FORWARD-LOOKING INFORMATION

This Annual Information Form contains, and Hydro One's oral and written public communications often contain, forward-looking statements that are based on current expectations, estimates, forecasts and projections about the business of Hydro One and the industry in which Hydro One operates and includes beliefs and assumptions made by the management of our company. Such statements include, but are not limited to, statements about the general development of our business; statements about the IPSP and projects flowing therefrom; statements about smart meters including their capabilities, costs, cost recovery and deployment and/or implementation plans; expectations regarding the Cornerstone project; the expected impact of CDM programs; expectations regarding connections of new generation to our transmission and distribution systems; the expected expiry of the electricity transfer tax exemption; statements about our strategy; expectations regarding the impact of the proposed *Green Energy and Green Economy Act, 2009* on our company; statements regarding future capital expenditures and our capital and other investment plans; statements regarding the reliability of our distribution and transmission systems including equipment performance; expectations regarding load growth and new generation; the expected completion of projects related to interconnection capacity; statements about effective dates of cyber-security standards; statements about initiatives to attract and retain staff; statements about the end of term of our outsourcing arrangement; expectations regarding environmental expenditures and other environmental matters including the expected cost increases resulting from new PCB regulations and the need for environmental approvals and assessments; the expected impact on transmission and distribution rates resulting from our rate applications; expectations regarding developments in the statutory and operating framework for electricity distribution and transmission in Ontario including changes to codes, licences, rates, rate orders, cost recovery, rates of return and rate structures in both our transmission and distribution businesses and the timing of decisions from

the OEB; expectations regarding our strategy for acquisitions or divestitures of distribution assets; the possibility of the Province making declarations pursuant to our memorandum of agreement with them; expectations regarding workforce demographics; expectations regarding borrowing requirements; the estimated impact of changes in the forecast long-term Government of Canada bond yield (used in determining our regulated rate of return) on our net income; the estimated impact of changes in interest rates on our net income; expectations regarding anticipated expenditures associated with transferring assets located on Indian lands; statements regarding provincial ownership of our transmission corridors; expectations regarding future pension contributions; our expectation regarding our need for the OEFC indemnity associated with the original transfer orders; and legal proceedings in which we are currently involved. Words such as "expect," "anticipate," "intend," "attempt," "may," "plan," "will," "believe," "seek," "estimate," and variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve assumptions and risks and uncertainties that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed, implied or forecasted in such forward-looking statements. Hydro One does not intend, and Hydro One disclaims any obligation to update any forward-looking statements, except as required by law.

These forward-looking statements are based on a variety of factors and assumptions including, but not limited to: no unforeseen changes in the legislative and operating framework for Ontario's electricity market; favourable decisions from the OEB and other regulatory bodies concerning outstanding rate and other applications; no unforeseen changes in rate orders or rate structures for our distribution and transmission businesses; a stable regulatory environment; and no significant event occurring outside the ordinary course of business. These assumptions are based on information currently available to Hydro One including information obtained by Hydro One from third-party sources. Actual results may differ materially from those predicted by such forward-looking statements. While Hydro One does not know what impact any of these differences may have, its business, results of operations, financial condition and its credit stability may be materially adversely affected. Factors that could cause actual results or outcomes to differ materially from the results expressed or implied by forward-looking statements include, among other things:

- the risks associated with being controlled by the Province including the possibility that the Province may make declarations pursuant to our memorandum of agreement with it, as well as potential conflicts of interest that may arise between us, the Province and related parties;

- public opposition to and delays or denials of the requisite approvals and accommodations for projects necessary to increase transmission capacity;

- the risks related to our work force demographic and our potential inability to attract and retain qualified personnel;

- the risks associated with the execution of our capital and maintenance programs necessary to maintain the performance of our aging asset base;

- the risks associated with being subject to extensive regulation including risks associated with OEB action or inaction;

- the timing and results of regulatory decisions regarding our revenue requirements, cost recovery and rates;
- the potential impact of CDM programs on our load and our revenues;
- the risks of counter-party default on our outstanding derivative contracts;
- the risks associated with changes in interest rates or discount rates;
- the risks associated with changes in the forecast long-term Government of Canada bond yield;
- the risk that we are not able to arrange sufficient cost effective financing to repay maturing debt and to fund capital expenditures and other obligations;
- the potential impact of not being able to recover our pension costs;
- future interest rates, future investment returns, changes in benefits and changes in actuarial assumptions;
- the risk to our facilities posed by severe weather conditions, natural disasters or catastrophic events and our limited insurance coverage for losses resulting from these events;
- the risk that we may incur significant costs associated with transferring assets located on Indian lands;
- the risks associated with maintaining a complex information technology system infrastructure and transitioning most of our financial and business processes to an integrated business and financial reporting system;
- the potential for substantial and currently undetermined or underestimated environmental costs and liabilities;
- the inability to negotiate collective agreements consistent with our rate orders or in a timely fashion and the potential for labour disputes;
- the potential that we may incur significant expenses to replace some or all of the functions currently outsourced if our agreement with Inergi LP is terminated;
- the impact of the ownership by the Province of lands underlying our transmission system;
- the potential impact of not being able to recover all of our project costs associated with the installation of smart meters;
- the impact of the proposed *Green Energy and Green Economy Act, 2009* on our company and the costs and expenses arising therefrom; and
- the content and timing of the revised and final IPSP, as approved by the OEB.

Hydro One cautions you that the above list of factors is not exclusive. Some of these and other factors are discussed in more detail under "Risk Factors" in this Annual Information Form. You should review the section entitled "Risk Factors" in detail.

GENERAL DEVELOPMENT OF THE BUSINESS

We are wholly owned by the Province and our transmission and distribution businesses are regulated by the OEB. Our industry, including our company, is governed within the broad legislative framework of the *Electricity Act, 1998*, as amended, and the *Ontario Energy Board Act, 1998*, as amended.

Regulated Price Plan Structure

On April 1, 2005, the OEB implemented a regulated price plan structure for the cost of electricity supplied to low volume and designated customers ("RPP"). The RPP regulates only the commodity price of electricity and does not affect the rates charged for transmission and distribution of electricity. The RPP also introduced seasonal consumption thresholds. For residential customers, the price threshold between the lower tier price and the upper tier price is 600 kWh per month in the summer and 1,000 kWh per month in the winter. For non-residential customers, the price threshold between the lower tier price and the upper tier price is 750 kWh per month in both the summer and the winter. A summary of some recent prices set by the RPP follows:

RPP Pricing		
Winter (Nov. 1, 2007 – April 30, 2008)	Lower Tier Price	5.0 cents
	Upper Tier Price	5.9 cents
Summer (May 1, 2008 – Oct. 31, 2008)	Lower Tier Price	5.0 cents
	Upper Tier Price	5.9 cents
Winter (Nov. 1, 2008 – April 30, 2009)	Lower Tier Price	5.6 cents
	Upper Tier Price	6.5 cents

Prices under the RPP are reviewed and are subject to change every six months based on an updated OEB forecast and any accumulated differences between the amount that consumers paid for electricity and the amount paid to generators in the previous period.

Ontario Power Authority

The Ontario Power Authority (OPA) was created by statute in 2004 under the *Electricity Restructuring Act, 2004*, and its objects are defined in Part II.1 of the *Electricity Act, 1998*.

It is a non-profit corporation without share capital, and it is licensed and regulated by the OEB. The OPA's mandate is to ensure the adequacy and efficiency of electricity supply in Ontario through planning of electricity supply and demand.

On August 29, 2007, the OPA filed its first IPSP with the OEB for approval.

The Minister of Energy and Infrastructure issued a directive to the OPA on September 17, 2008 requiring the OPA to revisit the IPSP with a view to establishing new targets in a number of areas including renewable energy sources and conservation. The directive also asks the OPA to undertake an enhanced process of consultation with First Nations and Métis communities in light of potential duty to consult obligations. As a result of the Minister of Energy and Infrastructure's directive, the OEB adjourned its review of the IPSP on October 2, 2008, until further notice.

Smart Meters

The *Energy Conservation Responsibility Act, 2006* provides the framework for the installation of smart meters in all homes and small businesses in Ontario by December 31, 2010. Electricity distributors are accountable for the deployment of smart meter infrastructure and related technology for communications to meet "minimum requirements" as defined in the regulations. The Province has now appointed the IESO to be the entity whose mandate includes the storage of all provincial hourly data. Distributors are also expected to be accountable for the implementation of time of use rates that is at present voluntary.

Hydro One Networks Inc. and Hydro One Brampton Networks Inc. have installed approximately 780,000 smart meters to date as of the end of 2008. These meters are expected to be capable of measuring and reporting usage over predetermined periods, being read remotely, and, when combined with the systems being provided by the IESO, will be capable of providing customers with access to information about their electricity consumption on a daily basis. Smart meters are regarded by the Province as an integral means of promoting a culture of conservation.

Smart meter activities continue to progress according to plan. The current state of smart meter and communication technology remains somewhat dynamic; however we have been able to complete the majority of testing, including rural applications. Total project costs continue to be significant with expenditures in 2008 amounting to approximately $119 million and planned expenditures in 2009 expected to amount to approximately $175 million; however both the financial estimates as well as estimates related to deployment times are subject to potential variation.

On March 21, 2006, the OEB approved an initial monthly funding rate of $0.27 per metered customer per month, effective May 1, 2006. Effective May 1, 2007 this rate was increased to $0.93 per metered customer per month for Hydro One Networks Inc. Effective May 1, 2007, Hydro One Brampton Networks Inc.'s smart meter rate was increased to $0.67 per metered customer per month from $0.28 per metered customer per month. On August 8, 2007 the OEB issued a decision that allowed us to reduce our net smart meter regulatory asset and record fixed assets. On December 18, 2008, the OEB issued a further decision for Hydro One Networks Inc. that approved costs incurred to December 31, 2007 and further advised that ongoing costs in 2008 should continue to be tracked in deferral accounts for future filing and recovery.

There may be an opportunity to leverage the smart meter infrastructure for smart network initiatives such as in-home displays, load control, distribution operations automation and mobile technology. The benefits of a smart network will be assessed and included in our future investment plan as appropriate.

Cornerstone

Cornerstone is a project being undertaken by our company for the planned, phased replacement of key enterprise Information Technology (IT) systems in Hydro One that have reached "end-of-life". As well, Cornerstone is designed to transform business processes to realize value from new key enterprise IT systems and continue to meet business requirements. Together, the new enterprise IT systems and transformed business processes are expected to enable Hydro One to deliver efficiency gains back into the business.

Conservation and Demand Management

The Province has established specific provincial targets for CDM and Hydro One's distribution businesses have built expenditures into their plans to help meet these targets. In May 2004, the Province authorized local distribution companies, including Hydro One, to apply to the OEB for the third installment of their allowable return on equity beginning March 1, 2005. The Province also indicated that the approval of the OEB would be conditional on a financial commitment to reinvest an amount equal to one year's worth of the incremental returns in CDM initiatives. For Hydro One Networks Inc. and Hydro One Brampton Networks Inc., the total after-tax CDM revenue available at that time was approximately $42.7 million. Hydro One submitted CDM plans for this full amount to the OEB on January 11, 2005. On February 18, 2005, Hydro One received approval of its CDM plan on behalf of Hydro One Networks Inc. on the condition that, among other things, planned spending on smart meters for 2006 ($7.1 million) be redirected to other projects. On November 1, 2005 the revised plan was approved as filed, enabling total expenditures of $39.5 million. On February 18, 2005, Hydro One Brampton Networks Inc.'s plan for $3.2 million in CDM spending was also approved as filed. On February 2, 2005, Hydro One Remote Communities Inc. received interim approval, as requested, for a CDM plan for $300,000. The OEB requires each distributor to file an annual report, including a cost-benefit analysis by March 31 of each year in respect of the results of the previous year. Hydro One Networks Inc.'s expenditures of $39.5 million were completed by April 2008 in conformance with the revised plan. Hydro One Brampton Networks Inc.'s planned spending is complete.

On July 13, 2006, the Ministry of Energy issued a directive to the OPA regarding the OPA assuming responsibility for organizing the delivery and funding of CDM programs through electricity distributors in Ontario. The directive recognized that distributors have a role as delivery agents for CDM and that funding for their programs should be secure, stable and multi-year.

The directive provides guidance on key funding aspects of CDM for distributors as follows:

1. The OPA will begin organizing the delivery and funding of CDM programs through distributors, with implementation of funding to occur in the earliest practical timeframe.

2. The funding will be limited to a total of $400 million over three consecutive years.

3. Distributors would contract to deliver programs funded by an OPA-administered distributor fund on a non-competitive basis in their service territory.

4. These funds will not include provisions for smart meters.

5. The OPA should support the OEB in its continuing efforts to reduce barriers to CDM including decreases in revenues due to distributors' conservation programs.

On November 2, 2008, the OPA filed with the OEB its proposed 2009 expenditure and revenue requirement and fees for review pursuant to subsection 25.21 of the *Electricity Act, 1998*. Included in this application are the CDM programs intended for implementation by local distribution companies such as Hydro One. The application also seeks approval for recovery of the expenditures for these programs.

Procurement of New Generation

The OPA continues to procure, and have plans for further procurement, of new, cleaner and renewable generation in Ontario. This is reflected in the Minister of Energy and Infrastructure's September, 2008 directive to the OPA to review the IPSP with a view to (among other things) enhancing the amount and diversity of renewable energy sources in the supply mix, improving transmission capacity in Northern Ontario and other parts of Ontario, and increasing the availability of distributed generation and in the introduction of Bill 150, *The Green Energy Act and Green Economy Act, 2009* on February 23, 2009. See "Recent Developments: Green Energy and Green Economy Act, 2009" for further information. Hydro One continues to work with successful proponents under various OPA procurements of new generation. Hydro One has placed a high priority on connecting these new sources of supply reliably to our transmission and distribution systems in a timely fashion.

Almost 500 new renewable generation connections to our distribution system have been assessed. Although a backlog of applications remained as of year end, Hydro One has dedicated significantly more resources to this work, which is expected to lead to eventual elimination of the backlog.

Hydro One has just completed technical connection standards and a workshop with generation proponents to discuss these standards and other issues of concern. Further, Hydro One has identified options for investments in infrastructure required to enable substantially more new generation to connect reliably and effectively and these options are now undergoing further planning. The options ultimately chosen will be submitted for review as necessary by other agencies, primarily the OEB and OPA.

Hydro One is working proactively with the Ministry of Energy and Infrastructure, the OPA, the OEB and the IESO to develop strategies and processes to address the need for additional generation, and in particular, the impact on Hydro One's networks. See "Risk Factors – Risks Associated with Transmission Projects."

Hydro One Networks Inc. had filed an application with the OEB for an exemption from certain timelines prescribed in the Distribution System Code related to proposed connections of generation facilities to the distribution system. By way of an interim order, the OEB granted Hydro One Networks Inc. an exemption from those timelines from June 27, 2008 until the final

disposition of the proceeding, and subsequently, on December 10, 2008, temporarily adjourned the proceeding.

Electricity Transfer Tax Exemption

In October 2006, the Province announced that publicly-owned utilities will be exempt from paying the electricity transfer tax when they sell electricity distribution assets to other publicly-owned utilities in Ontario. The normal transfer tax payable is equal to 33% of the fair value of the municipality's interest in electricity assets transferred to another entity. The transfer tax exemption became effective on October 17, 2006 and was to last for two years. The transfer tax exemption was extended for one year and will now expire on October 17, 2009. The Province indicated that the transfer tax exemption is designed to encourage efficiencies and promote consolidation among Ontario's publicly-owned electricity utilities. The Province also has lifted the moratorium on the purchase and sale of electricity distribution assets by Hydro One, with the understanding that any future asset purchases or dispositions help further overall efficiency in the sector. We have and will actively seek strategic opportunities for acquisitions or divestitures, on a voluntary and commercial basis, where they are consistent with our vision and direction from our shareholder. Our investment plan does not include any funding for LDC acquisitions or divestitures.

Agency Review Panel

The Agency Review Panel ("Panel") was established on January 29, 2007 to review specific issues concerning Hydro One, the IESO, the OPA, OPG and the OEB (collectively, the "Institutions"). The Panel was asked to take an in-depth look at overall compensation for top executives of the Institutions and to report back to the Province on areas where energy sector effectiveness can be further strengthened, including assessments of overlap and duplication between agencies, and whether sufficient steps are being taken to address concerns about potential shortages of skilled workers in the future.

In May 2007 the Panel submitted its report concerning executive compensation at the Institutions. The Minister of Energy subsequently announced that all the recommendations of the Panel were being accepted by the Province and requested us to support the initiative. Hydro One has complied with the relevant recommendations. Some of the key recommendations included:

- Compensation should reflect the mixed commercial and public interest nature of the jobs at these Institutions.
- Using a more appropriate model for setting executive compensation that will result in reduced compensation for top executives at OPG and Hydro One.
- Further enhancing the executive salary disclosure system to make it more accessible and transparent by including the rationale for executive compensation decisions.
- Discouraging the use of perquisites for executives.

With the exception of the enhanced salary disclosure system, the recommendations cited above would apply upon the replacement, at the time of retirement, resignation, or otherwise, of the current incumbents or upon negotiation of new contracts to be entered into at the time of the

expiry or renegotiation of the contracts of the current incumbents. For further information on compensation, please see "Statement of Executive Compensation – Elements of Compensation – Current Methodology".

In November 2007 the Panel submitted its report concerning energy sector effectiveness and human resource challenges. The Panel provided several recommendations but found overall that Ontario's electricity sector and the provincial agencies within it appear to be functioning reasonably well. Key recommendations included:

- Combining the balance of the functions of the OPA with those of the IESO into a combined agency when it seems reasonable to the Minister to do so, but probably not before the OEB has completed its current review of the initial IPSP.

- Hydro One and IESO working together to develop a uniform approach to connection assessments that is consistent with the requirements of the Transmission System Code in order to reduce overlap, duplication and inefficiencies, for the benefit of existing and potential customers.

- Establishing an understanding or protocol among the various ministries and regulatory tribunals to create, on a temporary basis and using existing legislation, a single integrated approvals process for electricity projects based upon existing legislative authorities to ensure the timely consideration of urgent projects set out in the IPSP or otherwise.

- Enacting legislation that would create a single integrated approvals process for electricity projects on a permanent basis.

- Continuing the independence of Ontario's Chief Energy Conservation Officer to ensure regular reports on Ontario's conservation progress.

- Creating new tools to ensure a continued and growing supply of expertise and skilled workers to meet the needs of Ontario's energy future.

- Continuing to facilitate the consolidation of local distribution companies, which deliver electricity to homes and businesses.

DESCRIPTION OF THE BUSINESS

Overview

We are the largest electricity transmission and distribution company in Ontario. We own and operate substantially all of Ontario's electricity transmission system, accounting for approximately 96% of Ontario's transmission capacity as measured by revenues for the year ended December 31, 2008. Our transmission system is one of the largest in North America based on assets. Our distribution system is the largest in Ontario based on assets, and spans approximately 75% of Ontario, serving approximately 1.3 million customers. We have three reportable segments: (1) our transmission business; (2) our distribution business; and (3) our other business.

Our transmission business, which represented approximately $7.88 billion of our total assets of $13.88 billion as at December 31, 2008, transmits electricity through an approximately 29,000 circuit-kilometre high-voltage network. We transmit electricity from generators to our own distribution networks, to 51 local distribution companies and to 63 large industrial customers directly connected to our transmission system. We also own and operate 26 facilities that interconnect our transmission system with systems in neighbouring provinces and states.

Our distribution business, which represented approximately $5.87 billion of our total assets of $13.88 billion as at December 31, 2008, distributes electricity through our approximately 123,000 circuit-kilometre low-voltage distribution system, to municipalities and to rural areas. Customers of our distribution business include 32 local distribution companies that are not directly connected to our transmission system, 47 large industrial customers and approximately 1.3 million rural and urban customers. Hydro One Brampton Networks Inc. is our urban distribution company, serving approximately 130,000 customers in the GTA with approximately 2,700 circuit-kilometres of lines. We also operate through our subsidiary, Hydro One Remote Communities Inc., 18 small, regulated generation and distribution systems in 20 remote communities across Northern Ontario that are not connected to Ontario's electricity grid.

Our other business segment is primarily represented by the operations of Hydro One Telecom Inc. This subsidiary markets dark and lit fibre-optic capacity to telecommunications carriers and commercial customers with broadband network requirements. The assets of this segment constituted approximately $126 million of our total assets of $13.88 billion as at December 31, 2008.

The OEB regulates our transmission and distribution businesses and issues rate orders to establish the revenue requirements required to cover the approved costs of these businesses plus a specified rate of return.

Recent Developments

Hydro One Chair of Board of Directors

On December 8, 2008, James Arnett, Chair of the Board of Directors, resigned as a director and as Chair following his appointment as Special Advisor to the Government of Canada and the Province on the auto sector's restructuring plans and Douglas Speers was appointed as Chair, on an interim basis until Mr. Arnett's return. Having resigned as a Special Advisor to the Government of Canada, Mr. Arnett was re-appointed as Chair of the Board of Directors effective February 17, 2009.

New Chief Financial Officer

On February 3, 2009, Hydro One announced the appointment of Sandy Struthers as its new Chief Financial Officer effective February 12, 2009. Beth Summers resigned as Chief Financial Officer effective the same date.

Change in Executive Officers

On March 1, 2009 Geoff Ogram assumed the newly-created role of Special Advisor to the President, and, in addition to his former role as Vice-President, Corporate Projects, Carmine Marcello assumed the role of Vice President, Asset Management.

Green Energy and Green Economy Act, 2009

On February 23, 2009, the Province introduced Bill 150, the *Green Energy and Green Economy Act, 2009*, which is an omnibus bill containing the *Green Energy and Green Economy Act* itself and 12 Schedules, the first of which is the stand-alone *Green Energy Act, 2009* (the "Green Energy Act"). The remaining schedules contain consequential amendments to other legislation affected by the Green Energy Act, in particular, the *Electricity Act, 1998*, the *Ontario Energy Board Act*, the *Environmental Protection Act* and the *Planning Act*. The Green Energy Act and the amendments to other statutes leave many of the implementation details to future regulations.

The object of the proposed Green Energy Act is to promote renewable energy projects and a green economy as well as to expand energy conservation and energy efficiency.

To achieve the renewable energy projects goal, the legislation creates within the Ministry of Energy and Infrastructure a renewable energy facilitation office supervised by a renewable energy facilitator. The facilitator's role is to assist proponents of renewable energy projects in developing their projects through work with other ministries in obtaining required approvals.

There is now proposed a provision for a feed-in tariff program to be established by the Minister of Energy and Infrastructure and administered by the OPA. This program includes a procurement process, standard program rules, standard contracts, standard pricing regarding classes and the manner by which the generation facility is used, deployed or installed. The goals under the feed-in tariff program include the Province's desire to promote participation by aboriginal peoples in the development and establishment of renewable energy projects as well as the involvement of local communities and the promotion of domestic content in the projects.

By way of amendment to several statutes, a more streamlined approvals process is established for renewable energy projects in order to avoid duplication of applications such that a renewable energy approval will replace certificates of approval under the *Environmental Protection Act* and will replace other approvals or permits under other legislation, including existing municipal approvals. The amended *Electricity Act, 1998* will provide for mandatory priority connections of renewable energy generation facilities to the transmission or distribution system where the applicable technical, economic and other prescribed or mandated requirements are met. Transmitters' and distributors' licences granted by the OEB will be deemed to contain a condition requiring priority connection access. To ensure that renewable energy projects can be accommodated, transmitters, distributors, the OPA and the IESO will be required to provide prescribed information about the ability of distribution or transmission systems to accommodate renewable energy projects.

The "smart grid" has also been highlighted in the amendments to the *Electricity Act, 1998*. The smart grid is to provide technology to enable the increased use of such renewable energy sources and technology. As well, the enhanced opportunities for demand response, price information, load control and innovation are to be provided through the implementation of the smart grid. A

licensee will be required to submit plans for approval by the OEB for development and implementation of investments in the smart grid.

Also, public agencies, which are government ministries or such entities as may be prescribed by regulation as a public agency, will be required to submit conservation and demand management plans, with the intention of meeting prescribed targets. Public agencies shall consider, and may implement, energy conservation and efficiency when purchasing goods or making capital investments. Prior legislation dealing with energy conservation and efficiency is to be repealed and substituted by this legislation. The office of the Conservation Bureau, within the OPA, will be eliminated.

Clearly noted in the proposed Green Energy Act is the requirement to interpret the legislation in a manner consistent with the duty to consult aboriginal peoples. This is further amplified in the amendment to the *Electricity Act, 1998* amending sections relating to the OPA and requiring the OPA to implement procedures for consulting aboriginal peoples for the procurement of electricity supply, how the consultation shall occur, and the timing of the consultation. Additionally, the OPA is to establish measures to facilitate the participation of aboriginal peoples in the development of renewable energy facilities and may include funding for aboriginal peoples to allow them to so participate.

Hydro One anticipates that it will be required to make significant investments in its transmission and distribution assets in order to comply with the aims and objectives of the proposed Green Energy Act.

Our Strategy

Hydro One's corporate strategy is based on our mandate, vision and values. Our mandate is to provide safe, reliable and cost effective transmission and distribution of electricity to Ontario electricity users. Our vision is to be the leading electricity delivery company in North America. Our values include safety, stewardship, excellence and innovation. We are committed to providing innovation and leadership in renewing Ontario's power grid. To that end, we have identified eight strategic objectives:

- *Creating an injury-free workplace and maintaining public safety.* We continue to focus on creating a passion for preventing workplace injuries and ensuring public safety.

- *Satisfying our customers.* In order to satisfy our customers, we focus on the reliability and quality of power delivery, delivering on commitments we make to our customers, providing value for money, partnering with the communities we serve, communicating effectively with our customers and building our reputation as a trusted steward of provincial transmission and distribution assets.

- *Continuous innovation.* We are committed to identifying and providing innovative solutions that improve the reliability and efficiency of electricity delivery and allow our customers more capability to manage their power costs.

- *Building and maintaining reliable, cost-effective power delivery systems.* Our transmission strategy is to provide a robust and reliable provincial grid that

accommodates the Province's emerging generation profile and demand requirements. Our distribution strategy entails providing greater visibility, increased control and improved customer service through smart grid technology, while continuing to provide reliable service at an affordable cost over a wide range of geography and climate.

- *Protecting and sustaining the environment.* We play a central role in reducing Ontario's carbon footprint, both through the delivery of clean and renewable energy and through measures that allow our customers to manage and reduce their energy use.

- *Skill development and knowledge retention.* We are addressing our demographic challenges through a comprehensive program of recruitment, training in core competencies, staff development and knowledge transfer.

- *Maintenance of a commercial culture that increases value for our shareholder.* We are committed to operating on a financially sustainable basis and to increasing the value of our assets.

- *Productivity improvement and cost-effectiveness.* To achieve our vision as the leading electricity delivery company in North America, we constantly strive to be the most productive through efficiency improvements and effective management of costs. Our goal is to be top quartile in key unit cost metrics relative to our North American electricity industry peer group.

Hydro One recognizes the pivotal role innovation will play in building a smart electricity grid that supports high quality jobs and a clean environment for Ontario. We are committed to becoming the industry leader in putting innovative solutions to work for the well-being of the Ontario economy and its citizens.

Our Transmission Business

Overview

Our transmission system operates at 500 kV, 230 kV and 115 kV and transmits electricity to customers consisting of 51 local distribution companies, our own distribution businesses and 63 large industrial companies that have loads greater than 5 MW. Electricity is also delivered to utilities in other jurisdictions through inter-ties. Electricity is supplied through generator supply contracts, both within and outside Ontario, of which 93 in Ontario are connected directly to the transmission grid. Our transmission system serves over four million customers, directly or indirectly, and transported approximately 148.7 TWh of energy throughout Ontario in 2008. Revenues from our transmission business accounted for approximately 26% of our total revenues in 2008 and approximately 27% of our total revenues in each of 2007 and 2006, respectively.

Our transmission system forms an integrated transmission grid that can be divided into two components based on function. The integrated network, or bulk system, operates primarily at 500 kV or 230 kV over relatively long distances and links major sources of generation to transmission stations and larger area load centres. The area supply system operates at 230 kV or 115 kV and links the bulk system to local generators and loads, such as local distribution companies, industrial customers and our own distribution operations. Transformer stations

located near load centres step down the high voltage to the level required for retail distribution systems or end-use customers connected directly to our transmission system.

Our transmission system is interconnected with the North American eastern system that is comprised of virtually all of the electric utilities east of the Continental Divide. Our transmission business owns and operates 26 inter-ties at 345 kV, 230 kV, 115 kV and 69 kV levels with New York (9), Québec (9), Michigan (4), Manitoba (3) and Minnesota (1). The two 69kV New York inter-ties are operated in idle mode at this time. Due to the nature of the system, the current interconnections with Québec are operated in a radial connection mode where load and/or generation is connected to either the Ontario system or the Québec system at any one time, but not to both simultaneously. The new interconnection with Quebec, expected to be placed in service in 2009, will enable the Ontario and Quebec systems to be operated in a "tied" or "parallel" mode.

Through these 26 interconnections, we can accommodate imports of about 4,000 MW and exports of approximately 5,800 MW of electricity. In operation, the actual import and export capabilities may be restricted significantly by limitations within our or another jurisdiction's transmission networks, unscheduled power flows between interconnected systems and local load and generation patterns.

Our transmission system is currently relatively free of restrictions in its ability to supply electricity to major load centres from generating sources located across Ontario, although there are certain short duration periods when the transmission constraints restrict economical utilization of generation. A 500 kV system serves as the transmission "backbone" around the GTA with 500 kV connections to Northern Ontario, Ottawa, London and the major generating facilities in Ontario. As new generation projects are assessed in Ontario, the impact on the transmission system is assessed and where required, transmission investment plans are initiated in a timely manner.

Transmission Planning

Hydro One develops transmission plans for new transmission facilities and for refurbishment and replacement of existing transmission facilities, as required. The plans for new facilities identify proposed equipment, configuration, routing and resulting capacities for network, local area and connection/transformation investments. We also consult with customers to determine the need, timing and technical solutions for new connection/transformation facilities. We consult with affected communities, stakeholders and First Nations and Métis as part of the project development process for new or upgraded transmission lines.

The need for additional network and local area capabilities is determined in consultation with the OPA (which plans future generation and CDM programs) and customers. The longer term transmission plans to enhance network capability are identified formally in the OPA's IPSP. The need for near term and long term solutions may also be highlighted in the reliability reports issued by the IESO. The IESO assesses the system impact of proposed facilities based on requests by Hydro One, as required by the Market Rules. Projects involving new transmission lines longer than 2 kilometres are subject to the OEB's approval. A Transmission Line or Transmission Station as prescribed in Ontario Regulation 116/01 made under the Environmental Assessment Act is subject to the Environmental Screening Process, as defined in the Regulation, and is subject to Class Environmental or full Environmental Assessment approval.

Hydro One's plans to maintain, refurbish or replace existing facilities are developed on the basis of maintenance standards, asset condition assessments and end-of-life criteria specific to each type of equipment. Priorities are assigned to each type of investment based on the risks that it mitigates. These investment plans are also included in our rate filings submitted to the OEB.

Transmission Capital Expenditure Plans

Transmission system capital expenditures are anticipated to be significant over the 2009 to 2011 period, amounting to about $3.0 billion overall with $950 million expected to be spent in 2009. Our capital investment plan is designed to address Ontario's changing generation profile and accommodate load growth in areas throughout the province. Additionally, this plan seeks to sustain or improve our top quartile ranking for transmission reliability performance in North America for transmission systems of 230kV and above. This plan also furthers our ongoing objective of sustaining the performance of aging assets through refurbishment programs and end of life asset replacements. Hydro One anticipates that it will also be required to make significant investments in its transmission assets in order to comply with the aims and objectives of the proposed Green Energy Act.

Major Transmission Capital Development Projects

- New 500kV Bruce to Milton Double Circuit Transmission Line

The IESO's December 2007 Ontario Reliability Outlook indicated that existing transmission in southern Ontario cannot accommodate the generation expected to come into service in the Bruce area over the next few years. The Province supported this view by stating that Hydro One should engage in "expanding the transmission capacity from Bruce County and surrounding area to facilitate the transmission of electricity from several new wind farms and the Bruce [nuclear] facility" (The Government of Ontario, *A Balanced Plan for Ontario's Electricity Future*). The OPA has determined that the preferred solution to increase the transfer capability of Hydro One's 500kV system is to build a new 500kV double circuit transmission line between the Bruce Nuclear Station and the Milton Switching Station to securely incorporate all eight units from the Bruce nuclear facilities and the committed and potential wind generation. The requisite OEB approval for the 500kV line has been obtained and approval under the *Environmental Assessment Act* is being sought.

- Install Seven 230kV Capacitor Banks in Southwestern Ontario

This project is in order to comply with the recommendation of the OPA to install seven 230kV shunt capacitor banks at three stations in southwestern Ontario in 2009 as a near-term measure to increase transfer capability in the Bruce Area and southwestern Ontario.

- Claireville TS to Cherrywood TS: Unbundle 500kV Circuits

The existing 500kV transmission lines between Cherrywood TS and Claireville TS in the Greater Toronto Area consist of two 500kV double circuit tower lines. In order to improve the reliability of the bulk electricity system, to provide greater operating flexibility, and to reduce the adverse impact on supply to customers, the two 'super' circuits will be unbundled. This will effectively result in two additional 500kV circuits between Cherrywood TS and Claireville TS. New 500kV terminations will be required at both Cherrywood TS and Claireville TS to accommodate the new circuits.

- Northeast Transmission Reinforcement: Installation of Static Var Compensators at Porcupine TS and Kirkland Lake TS

In order to mitigate concerns about increasing congestion on the interface between Northern Ontario and Southern Ontario and to enable renewable generation in Northern Ontario as per the Province's direction, the OPA has recommended near term measures to enhance the transfer capability between Northern Ontario and Southern Ontario and the transmission system north of Sudbury. These measures include the installation of a static var compensator ("SVC") at Porcupine TS and an SVC at Kirkland Lake TS. In-service is currently planned for late 2010.

- Southern Georgian Bay Transmission Reinforcement

Currently one 115kV single circuit line from Essa TS to Owen Sound TS provides the majority of electricity supply for load in the Southern Georgian Bay area of Ontario. In this area, a significant amount of load is exposed to rejection for a first contingency outage. As load in this area grows, it is increasingly exposed to load rejection. The existing 115kV single circuit between Essa TS and Stayner TS is being replaced with a double 230kV circuit along the existing right of way. Stayner TS will be converted from a 115kV station to a 230kV station. Transformation capacity at Stayner TS will also be increased. This project will improve transmission supply capacity, transformation capacity and customer reliability in the Southern Georgian Bay area while relieving other Simcoe County transformation stations to supply their own load growth.

- Woodstock Area Transmission Reinforcement

Customer load supplied in the Woodstock area of Southern Ontario at 115kV has exceeded the reliable transmission capacity. This project will increase transmission capacity through 11 km of new 230kV double-circuit line on the existing 115kV right-of-way between Ingersoll TS and a new station called Karn TS. The project also includes construction of the new Karn TS. These projects are expected to increase the transmission capacity in the Woodstock area to 290MW in preparation for future growth. In-service is currently planned for mid-2011.

Transmission Projects at the Local Load Connection Level

At the local load connection level, we continue to proactively address supply needs with our customers in order to meet their load growth. For projects required to provide reliable delivery of electricity to communities, the participation and support of the affected LDCs as partners in joint planning studies and throughout the consultation and approval processes continue to be essential. Examples of projects that are under construction to meet the growing needs of our customers include new transformer stations to serve Essex County and Simcoe County, and expansions of transformer stations serving Brampton, Kingston, York Region, Mississauga, Hamilton and Woodstock. To address other future needs of local load connections, we are in discussions with customers for major transmission expansions or new transformer stations and, where necessary, line connections in locations such as Mississauga, Oshawa and Brampton. Targeted investments in customer delivery point performance, power quality, and our 115 kV and 230 kV systems are expected to lead to improved reliability.

Transmission Sustainment

Our investment plan also includes increased program expenditures for sustainment initiatives to manage the replacement and refurbishment of our aging transmission infrastructure. Increased emphasis is being placed on those transmission assets that are critical to support generation facilities and the unrestricted transmission of energy to our customers. Targeted component replacement programs such as gas insulated switchgear, air blast circuit breakers, and transformers, as well as improved control initiatives to protect against animal contacts, have been adopted to remain in the top quartile in transmission reliability performance in North America.

Transmission Assets

Our transmission assets can be divided into four functional categories: transmission stations, transmission lines, network operations and telecommunication facilities.

Transmission Stations

Transmission station facilities are used for the delivery of power, voltage transformation and switching, and serve as connection points for both customers and generators.

Transmission stations can be broadly classified into two categories. The first category consists of terminal stations, including switchyards located at generating facilities, which are used mainly for switching and voltage transformation between the 500 kV, 230 kV, and 115 kV systems. The second category consists of customer supply stations, which are transmission stations that deliver power from the transmission system to wholesale customers. Currently, most transmission stations used for customer supply consist of paired circuits and step-down transformers that are meant to ensure that the failure of any one element will not result in a permanent loss of supply. For smaller or remote loads, a simpler station design with a single transformer or a single circuit is used.

Our transmission system includes 281 transmission stations whose components may include high voltage power transformers, power circuit breakers, high voltage switches, capacitor and reactor banks, protection and control systems, metering and monitoring systems together with site infrastructures such as buildings and security systems.

Transmission Lines

Our transmission lines are classified into bulk power lines and area supply lines. Bulk power transmission lines are main lines delivering power from generating stations or interconnections to receiving terminal stations. Bulk power transmission lines are part of the integrated transmission network and generally operate at 500 kV or 230 kV, with a few at 115 kV. Area supply lines take power from the transmission network at the receiving stations and transmit it to customer supply transformer stations at customer load centres. The usual voltage levels of area supply lines are 230 kV or 115 kV. All of these lines are overhead except for approximately 275 circuit kilometres of underground cables in urban areas.

The transmission system includes approximately 29,000 circuit kilometres of high voltage lines whose major components consist of cables, conductors, wood or steel support structures, foundations, insulators, connecting hardware and grounding systems

Network Operations

All of our transmission assets and many of our sub-transmission assets are managed from one location, the OGCC north of Toronto, Ontario. As owners and operators of the largest portion of the Ontario transmission network, we have the responsibility under the *Electricity Act, 1998* to ensure that our assets are operated in a safe and reliable manner which optimizes connection performance to our customers.

Accordingly, the OGCC is the controlling authority for the Hydro One transmission network and for large portions of the sub-transmission network. The OGCC reviews, approves, performs and/or authorizes all switching and control actions of our transmission system assets. In addition, the integrity of our transmission and much of our sub-transmission assets is continually monitored to ensure optimal performance of the network.

In addition, the OGCC coordinates planned distribution outages and is responsible for notifying affected customers. For forced outages, the OGCC creates outage tickets which contain all the relevant information for the outage, dispatches field crews and communicates estimated time of repair and confirms outage restoration with the Hydro One distribution customer.

The OGCC is fully supported by onsite customer service, engineering, operations technology, training, process and business planning staff. In addition to the OGCC, there is a fully functional back-up facility located in Toronto. The back-up facility would be staffed in the event of an evacuation of the OGCC.

Telecommunications Facilities

Our requirements for telecommunications include services for power system protection and operation, voice and administrative data. For power system protection and control as well as voice communications required for control of and repair to transmission and distribution assets, reliability and security requirements are very stringent and must continue to be met during prolonged blackout conditions. These telecommunications are vital to meeting our transmission reliability compliance obligations, ensuring the protection of our assets and ensuring efficient and rapid restoration following contingencies. These requirements are met through the use of our own facilities and services acquired from other telecommunications service providers. The reliability and availability of telecommunication services used in the protection and operation of our transmission system are vital to meeting our interconnection obligations, ensuring the protection of our assets and ensuring the reliability of our transmission system. Historically, if telecommunications service providers were not able or willing to provide the required services at an appropriate cost, we installed our own telecommunication facilities. These owned facilities include analogue microwave radio, fibre optic cable, power line carrier and mobile radio systems. The analogue microwave radio system reached the end of its useful life in the first half of this decade and a multi-year program to replace it with a digital fibre-optic and a digital microwave system was completed in 2007.

Projects Relating to Interconnection

Québec

Construction began in December 2006 on a new inter-tie with the Province of Québec that will increase our inter-tie capacity by approximately 1,250 MW. This consists of a new two-circuit 230 kV line between the systems near Ottawa, along with AC-DC-AC conversion facilities in Québec needed to connect the two systems in a continuous manner (currently, load or generation is required to be isolated to either system for import or export). Construction is on schedule, with the Ontario facilities having been completed late in 2008.The new facilities are expected to come into service in the second quarter of 2009 once construction and commissioning of the facilities in Québec are completed.

Michigan

Two of our interties with the State of Michigan have been upgraded with the installation of two, three phase shifting transformers and an autotransformer. The phase shifters were put into operation during emergency situations in 2005 and have been tested weekly since the fall of 2005. This equipment will provide greater control of the Michigan interties to manage power flows across the Ontario-Michigan border and indirectly across the Ontario-New York border. As a result, Ontario's export capacity will be increased by 1,000 MW and our import capacity by 500MW once they are fully operational.

An interconnection facilities agreement and associated operating procedures between Hydro One and Michigan's International Transmission Company (ITC) (the utility to which we are connected by these inter-ties) have been signed. The IESO and the Midwest Independent System Operator are finalizing their agreement in respect of this interconnection. Once this agreement is finalized, the current interconnection agreement made by Ontario Hydro will be terminated, and the phase-shifters will go into full operation. This is anticipated to occur in 2009.

Manitoba

Hydro One continues to work on options for a new tie between Ontario and Manitoba. Currently, work is underway on a potential option involving use of current rights of way held by a third party utility company. A new tie with Manitoba would likely require supporting agreements to be signed between appropriate entities in Manitoba and Ontario.

NERC (North American Electric Reliability Corporation) / NPCC (Northeast Power Coordinating Council)

In North America, standards to improve the reliability and security of the interconnected bulk electric system are developed by the NERC. The United States' Energy Policy Act of 2005 mandated compliance with these standards and assigned the Federal Energy Regulatory Commission ("FERC") as the regulatory agency that will approve and enforce these standards in the United States. Subsequently, FERC approved the establishment of NERC as an Electric Reliability Organization, with responsibility for developing reliability standards, monitoring compliance, assessing non-compliance, and applying sanctions for non-compliance. In 2007, FERC approved the first set of mandatory standards for which compliance and monetary sanctions came into effect on June 18, 2007.

In Ontario, the Market Rules mandate that we comply with the reliability standards established by NERC and NPCC, and our transmission licence mandates that we comply with the Market Rules.

NERC Critical Infrastructure Protection Standards

NERC Critical Infrastructure Protection ("Cyber Security") standards are expected to come into effect during the 2009-2010 timeframe. The standards are designed to ensure that utilities and other users, owners, and operators of the bulk power system in North America have appropriate procedures in place to protect critical infrastructure from cyber attack.

As a result, Hydro One's physical and information security processes are currently being upgraded to meet more stringent security requirements in order to meet the NERC requirement for auditable compliance by June 2010.

Hydro One expects to be fully compliant with the NERC requirements within the required time limits.

IESO

On September 22, 2006, Ontario Regulation 452/06, made under the *Electricity Act, 1998* came into force. The regulation provided that one of the objects of the IESO was to establish and enforce standards and criteria relating to the reliability of transmission systems.

Our Distribution Business

Overview

Our distribution systems provide customers with electricity distribution services through a low voltage distribution network. During 2008, approximately 30 TWh of electricity were delivered through the distribution system to approximately 1.3 million customers located in rural and urban areas (including approximately 130,000 urban retail customers located in Brampton, Ontario). The distribution systems also serve 32 local distribution companies that are not connected directly to our transmission system, another 36 local distribution companies that are connected to our transmission system and 47 customers with loads exceeding 5 MW. The distribution system comprises approximately 123,000 circuit kilometres of lines operating mainly at voltages of 50 kV or less and we own a total of 1015 distribution and regulating stations. Our distribution systems distribute electricity from our transmission system and 125 small embedded generators. Unlike the systems found in densely populated areas that are designed to include built-in redundancy, our distribution systems supply mainly rural areas with low population densities. To provide a cost effective service to these areas, the distribution systems are configured as a largely radial system, meaning that they are configured in straight lines, rather than loops, so that an outage at any point along the line causes all customers further down the line to lose power. As a result, component failures require immediate repair or replacement prior to service restoration. Revenues from our distribution business accounted for approximately 73% of our total revenues in 2008 and approximately 73% and 72% of our total revenues in 2007 and 2006, respectively.

Distribution Capital Expenditure Plans

Consistent with our approved distribution rate application, capital expenditures for our distribution business for the period 2009- 2010 are expected to focus on new load connections, trouble calls and storm damage, wood pole replacement, and system capability reinforcement. In response to the Province's initiatives to encourage renewable energy technologies, we are also

experiencing increased generation connection activity and are investigating potential major upgrades to the distribution system to accommodate this new generation. Distribution capital expenditures are focused on maintaining or improving (where it is feasible to do so) system reliability. This is accomplished through investments designed to preserve the performance of our aging distribution base, enhance operational flexibility and prevent equipment failures. Increasing investments are expected to be made within the distribution business, in particular reflecting increased wood pole replacements, feeder sectionalization and defect management. Across Ontario, we are continuing with the replacement of distribution assets that have reached their end-of-life elements, with installations that operate at higher voltage and conform to current standards. In addition, we expect to continue to construct new lines and stations in response to system growth forecasts or high load relief requirements, and expect to continue our efforts to make the distribution system more efficient.

In addition, we are continuing to implement initiatives to improve the reliability performance of our distribution system through improved maintenance and line clearing practices.

Distribution Assets

The electricity distribution system is made up of three system components: (i) low voltage lines connecting our transmission stations to our distribution stations and to some industrial customers and local distribution companies; (ii) distribution and regulating stations; and (iii) our distribution lines connecting the low voltage side of the distribution stations to industrial, commercial, farm, and residential customers as well as embedded local distribution companies. These system components include equipment such as poles, conductors, transformers, reclosers, protection devices and switches. Other assets include service centres and equipment, such as our transportation fleet, computing equipment and service and construction equipment.

Remote Communities

Through our subsidiary, Hydro One Remote Communities Inc., we operate 18 regulated generation and distribution systems across Northern Ontario which serve 20 remote communities that are not connected to Ontario's electricity grid, the facilities of which are owned either by us or by OEFC. These remote communities include a total of approximately 3,310 customers. Electricity used by these remote communities is produced by 54 installed diesel generators owned by us, which are supplemented by small amounts of wind or hydroelectric generation. Pursuant to Section 48.1 of the *Electricity Act, 1998* and Regulation 199/02 under the *Electricity Act, 1998* as later amended by Regulation 454/03, we are required, through one or more of our subsidiaries, to operate and maintain existing generation and distribution assets in, and supply electricity to, these remote communities.

Our Telecommunications Business

Our telecommunications business, which is carried on by our subsidiary, Hydro One Telecom Inc., markets dark and lit fibre optic capacity to telecommunications carriers and commercial customers with broadband network requirements. Hydro One Telecom Inc. leverages its parent company's telecommunications assets and delivers state-of-the-art, broadband telecommunications solutions to carriers, independent service providers, and large public and private sector customers.

Hydro One Telecom Inc. is a CRTC-registered, non-dominant, facilities-based carrier, providing broadband telecommunications services in Ontario with connections to Montreal and Buffalo, New York and Detroit, Michigan. Its fibre network spans over 4,000 kilometers.

Employees

At the end of 2008, our Hydro One Networks Inc. subsidiary had 4,714 regular (i.e., permanent) employees comprised of 567 non-represented executive and managerial staff, 3,202 employees represented by the Power Workers' Union and 945 employees represented by the Society of Energy Professionals. In addition, our Hydro One Brampton Networks Inc. subsidiary had 51 non-represented regular staff, 107 active employees represented by the Canadian Auto Workers and 42 employees represented by the International Brotherhood of Electrical Workers. We also had 1880 non-regular (i.e., temporary) employees comprised of 14 executive and managerial staff, 1019 employees represented by the Power Workers' Union, 71 employees represented by the Society of Energy Professionals and 776 employees represented by a combination of the Canadian Union of Skilled Workers (an electrical trade union) and the 16 construction building trade unions that have collective agreements with the Electrical Power Sector Construction Association. Hydro One Inc., Hydro One Remote Communities Inc. and Hydro One Telecom Inc. together have approximately 118 employees in total.

In 2008, we negotiated a three-year collective agreement with the Power Workers' Union which will expire on March 31, 2011. Also in 2008, we negotiated three-year agreements with the Canadian Auto Workers and the International Brotherhood of Electrical Workers in Brampton, both of which expire on March 31, 2011. Finally, we negotiated a three-year agreement with the Canadian Union of Skilled Workers which expires on April 30, 2011. See "Risk Factors – Labour Relations Risk."

We expect to continue to focus initiatives on the attraction and retention of staff and the maintenance and development of the skills and competence of all our employees to foster a productive work environment and to manage the impacts of anticipated retirements.

A key goal of ours is to manage the demographics of our workforce, an issue which we are monitoring, as the average age of our work force is over 46 years with approximately 18 years of service. In response to this issue, a comprehensive management development program, as well as a succession planning program, have been implemented. Pursuant to the succession planning program, active recruitment of new employees in key areas is underway. See "Risk Factors – Work Force Demographic Risk."

Outsourcing Arrangement with Inergi LP

Through our subsidiary Hydro One Networks Inc. we entered into an outsourcing services agreement with Inergi LP as of December 28, 2001. The provision of services by Inergi LP commenced on March 1, 2002. Inergi LP is an affiliate of CapGemini Canada Inc. Under the agreement, Inergi LP provides us with customer service operations and settlements, as well as supply management services, pay operations services, enterprise technology and finance and accounting services. As part of the agreement with Inergi LP, 906 of our unionized and non-unionized employees (including 770 regular and 136 non-regular employees) were transferred to Inergi LP on March 1, 2002. Under the agreement, we continue to make available, for use by the transferred employees, the assets used by them prior to the transfer of their employment, with refurbishments as needed.

The agreement has a 10-year term and has base service fees of approximately $1 billion over the term of the agreement. Fees are subject to decreases based on optional external benchmarking analyses every three years. Cap Gemini Ernst & Young US LLC has provided a financial guarantee, as well as a performance guarantee, of the obligations of Inergi LP. The performance guarantee covers the transition period in the event that the agreement is terminated. The agreement provides for rights of termination for each of the parties, including, on the part of our company, rights of early termination for convenience and upon the occurrence of specified business events. In such cases, we are obliged under the agreement to pay specified termination fees, as well as to contribute to resulting severance and other costs. In addition, upon expiration of the agreement, we have an obligation to contribute to employee severance costs, if any, up to a maximum amount of $10 million. The agreement expires on February 29, 2012. Given the complexities involved, we have begun developing a plan of action for end-of-term. See "Risk Factor – Risk Associated with Outsourcing Arrangement."

Financial

We aim to maximize the value of our company while maintaining an effective borrowing capability through stable credit quality and delivering stable financial returns to our shareholder.

We remain committed to understanding and staying abreast of best utility practices in order to execute our business in the most cost effective manner possible.

We believe that cost reductions and productivity improvements can be achieved through the joint management of our transmission and distribution businesses, the Inergi LP outsourcing arrangement pursuant to which we outsourced non-core functions to Inergi LP and the consolidation of our system operations functions. For example, we consolidated our system operations functions, which were previously dispersed across Ontario, into the OGCC while maintaining a back-up facility in Toronto. This initiative has produced lower costs and better service through the introduction of more technologically sophisticated operating tools.

Annual savings have been achieved in recent years as a consequence of our focus on operational excellence and these savings have largely been re-invested back into our work programs or have offset additional cost pressures. Going forward, we are continuing to focus on capital efficiency and workplace productivity, but additional savings opportunities are fewer, more complex and difficult to achieve.

Pension Plan

We established a defined benefit registered pension plan on December 31, 1999. Hydro One Inc. manages and invests the assets and liabilities of the pension fund as plan sponsor and administrator of the plan. As of December 31, 2008, there were 4,684 active members and 7,517 pensioners and disabled and deferred members. In accordance with the requirements of the *Pension Benefits Act* (Ontario), an actuarial valuation prepared as at December 31, 2006 was filed with the Financial Services Commission of Ontario on September 20, 2007. See "Risk Factors – Pension Plan Risk."

Effective December 31, 1999, we established the Hydro One Inc. Supplementary Pension Plan to provide supplementary pension benefits. On October 30, 2001, this plan was amended to require the establishment of a trust for the purpose of creating security for payment of the supplementary

pension benefits provided for therein. This trust was constituted as a Retirement Compensation Arrangement under the provisions of the *Income Tax Act* (Canada), and security was issued in the form of a letter of credit.

Insurance

We maintain insurance coverage, including liability, all risk property and boiler and machinery insurance. We also maintain other insurance coverage that is required by provincial statute, which covers automobile liability, pesticide liability and aircraft liability. We do not have insurance for damage to our transmission and distribution wires, poles and towers located outside our transmission and distribution stations including damage caused by severe weather, other natural disasters or catastrophic events or for environmental remediation costs. See "Risk Factors – Risk of Natural and Other Unexpected Occurrences."

Environmental

Although primarily regulated at the provincial level, jurisdiction over the environment is shared by Canadian federal, provincial and local governments. As a result, we are subject to extensive federal, provincial and local regulation relating to the protection of the environment that governs, among other things, environmental assessments, discharges to water and land and the generation, storage, transportation, disposal and release of various hazardous substances. See "Risk Factors – Environmental Risk."

Health Safety and Environmental Management System

As part of our Health, Safety and Environmental management system, Hydro One has an environmental management system designed to identify and assess the environmental effects of our operations and facilities and to aid in the continual improvement of our environmental performance. We continually update our environmental management system to reflect organizational changes and progress in achieving our environmental goals.

Permits, Licences and Approvals

We are required to obtain and maintain specified permits and approvals from federal, provincial and local authorities that relate to, among other things, waste disposal, drainage works and discharges to air and water.

A number of electricity projects we undertake or propose may require environmental approvals from the federal government or the use of federal lands, including reserves and other lands subject to the *Indian Act* (Canada), and will be subject to federal environmental assessment. Additional interconnection facilities with neighbouring utilities in other provinces and states require approvals and will be subject to federal regulatory review, which may include environmental assessment. Certain projects will also be subject to the provincial environmental assessment process. A significant number of our existing projects are subject to a streamlined environmental assessment process. The scope, timing and cost of environmental assessments at either the federal or provincial level depend on the type of project and its potential for environmental impact.

Releases

Federal, provincial and municipal environmental legislation operates to regulate the release of substances into the environment through the prohibition of discharges that will or may have an adverse effect on the environment. Spills and leaks of substances occur in the course of our normal operations. We could incur fines or clean-up costs in connection with these releases. Accordingly, we have spill, leak prevention and leak mitigation programs involving the testing, replacement, repair and installation of containment systems including regasketting of transformers and sulphur-hexafluoride filled equipment. In addition, we have an emergency response capability which we believe is sufficient to minimize the environmental impact of spills and to comply with our legal obligations.

Hazardous Substances

We manage a number of hazardous substances, such as polychlorinated biphenyls ("PCBs"), herbicides and wood preservatives. In addition, some facilities have substances present which are designated for special treatment under occupational health and safety legislation such as asbestos, lead and mercury. We have environmental management programs in place to deal with PCBs and herbicides.

PCBs

On September 17, 2008, Environment Canada published its final regulations governing the management, storage and disposal of PCBs. These regulations were enacted under the *Canadian Environmental Protection Act, 1999*. The new regulations impose timelines for disposal of PCBs based on different types of equipment, in-use status and PCB contamination thresholds. Under the regulations, all PCBs in concentrations of 500 parts per million (ppm) or more, except pole-top transformers and their pole-top auxiliary electrical equipment and light ballasts, must be disposed of by the end of 2009. PCBs in concentrations of 50 ppm or more in pole-top transformers and their pole-top auxiliary electrical equipment, light ballasts and other electrical equipment must be disposed of by the end of 2025. In addition, liquids with concentrations of 2 ppm or more that have been removed from equipment cannot be reused.

We have very limited PCB-contaminated assets in excess of 500 ppm. Our priority will be to target our inspection and testing work toward identifying and removing PCBs from these assets as quickly as operationally feasible. Assets to be disposed of primarily consist of pole and pad mount distribution transformers and light ballasts which require disposal by 2025. Contaminated distribution and transmission station equipment will generally be decontaminated by removing PCB-contaminated insulating oil and retrofilling with oil containing concentrations of less than 2 ppm as the liquids are removed.

Our best estimate of the total estimated future expenditures to comply with the final PCB regulations is about $305 million, an increase of about $265 million over the estimated amounts previously used to record the PCB portion of the environmental liability on our balance sheet. These expenditures are expected to be incurred over the period from 2009 to 2025 with the majority of the spending occurring in the 2013 to 2025 period. As a result of the final regulations and the resulting increase in expected future expenditures, in the third quarter of 2008, we increased our environmental liability as recorded on our balance sheet by approximately $195 million, the present value of the estimated increased future expenditures. As Hydro One

anticipates that the related expenditures will continue to be recoverable in future rates, a $195 million increase to the environmental regulatory asset was also recorded to reflect the probability of future recovery of these PCB expenditures from customers.

Estimated environmental liabilities are reviewed annually or more frequently if significant changes in regulation or other relevant factors occur. Estimate changes are accounted for prospectively.

Herbicides

We use herbicides primarily for the control of incompatible vegetation on rights-of-way, along distribution lines and on station sites. We currently use an integrated management approach toward vegetation management using manual and mechanical cutting, together with the selective use of herbicides. We are working with the Province to ensure our operations adhere to requirements under the proposed *Cosmetic Pesticides Ban Act* (Ontario) and associated regulations. As indicated below, the historical use of herbicides has contaminated some of our properties and some nearby properties.

Wood Preservatives

Wood preservatives are used in wood poles to protect the wood against fungi and insects and thereby extend their service lives. In the past, we have used poles which were impregnated with pentachlorophenol. We respond to contamination problems related to pentachlorophenol migration as they arise.

Land Assessment and Remediation

Hydro One Networks Inc. has a voluntary land assessment and remediation program in place to identify and, where necessary, remediate contamination related to our transmission and distribution stations, and service centres. Our Hydro One Remotes Communities Inc. subsidiary also has a program in place for generating stations it owns or operates. These programs involve the systematic identification of any contamination at or from these facilities and, where necessary the development of remediation plans for Hydro One and adjacent private properties. Potential contaminants include insulating oils, substances previously used for vegetation control such as arsenic trioxide, and other substances such as fuel oil, gasoline, PCBs and wood preservatives such as pentachlorophenol. Phase I assessments have been completed for most of the transmission stations, service centres and remote generating stations. Limited Phase I assessments were undertaken at distribution stations given their large number and similar operating history. Site screening involving on-site soil sampling at the areas of greatest potential for contamination have been undertaken at the majority of these sites.

The inventory of land in the program is approximately 1,562 sites. The number of sites where at least one soil or groundwater sample on site was found to be above the Ontario Ministry of the Environment standards (of at least one substance of concern) is 672. We have completed the clean-up of 161 sites, which include sites where underground fuel dispensing/storage tanks were removed. Further work may be required in the event we sell or decommission any of these sites. We have developed a risk-based property ranking system to assist in establishing priorities for Phase II sampling. This system is supplemented with visual inspections of the sites and nearby receptors. Remediation and/or risk management is occurring based on Phase II results and discussions with affected property owners and regulatory authorities. The Ontario Ministry of

the Environment (at the local and head office level) and local health departments/medical officers of health are actively involved in the program.

Future costs related to the land assessment and remediation program for Hydro One Networks Inc. are currently estimated at approximately $21.3 million over the next seven years. The estimated expenditure for 2009 is approximately $3.989 million.

Electric and Magnetic Fields

Electric and magnetic fields exist wherever electricity is used or transmitted, including electric power facilities such as transmission and distribution lines and substations, and within every building in Ontario that has electrical service. National and international health agencies, including the World Health Organization, have reported that the evidence is insufficient to conclude that the low levels of these fields in our communities have adverse effects on peoples' health. [1] Health Canada "does not consider guidelines necessary because the scientific evidence is not strong enough to conclude that typical exposures cause health problems." [2] We sponsor research and monitor national and international developments with respect to electric and magnetic fields. Public exposures to electric and magnetic fields are not currently regulated by either the federal or provincial governments and we are not aware of any current plans to regulate public exposures to electric and magnetic fields by these levels of government.

In 2008, the City of Toronto adopted an electric and magnetic fields prudent avoidance policy which requires us to incorporate practical low-cost measures to reduce electric and magnetic fields emissions when new transmission equipment is installed or existing equipment is modified. The policy also requires us to prepare a health impact assessment to evaluate options to minimize any increase to the yearly average exposure to electric and magnetic fields when new high-voltage transmission lines or increases in the capacity of existing transmission lines are proposed in that municipality.

Legal Proceedings and Regulatory Actions

In connection with the reorganization of Ontario Hydro, we have succeeded Ontario Hydro as a party to various pending legal proceedings relating to the businesses, assets, real estate and employees transferred to us. We will also assume responsibility for future claims relating to the businesses, assets, real estate and employees acquired by us and arising out of events occurring prior to, as well as after, April 1, 1999. In addition to claims assumed by us, we are, from time to time, named as a defendant in legal actions arising in the normal course of business. The pending legal proceedings, which include material claims to which we are currently a defendant, are discussed below.

On March 29, 1999 the Whitesand First Nation Band commenced an action in the Ontario Superior Court of Justice, naming as defendants the Province, the Attorney General of Canada,

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[1] E.g., World Health Organization (WHO). Electromagnetic Fields and Public Health. Fact sheet N°322 June 2007; Extremely Low Frequency Fields. Environmental Health Criteria, Vol. 238. Geneva, WHO, June 2007.

[2] Health Canada. It's Your Health: Electric and Magnetic Fields at Extremely Low Frequencies. http://www.hc-sc.gc.ca/iyh-vsv/environ/magnet_e.html

Ontario Hydro, OEFC, Ontario Power Generation Inc. and our company. On May 24, 2001, the Whitesand First Nation Band issued an almost identical claim against the same parties. The reason for the second claim is the procedural defence of the Province that proper notice of the first claim was not given under the *Proceedings Against the Crown Act* (Ontario). These actions seek declaratory relief, injunctive relief and damages in an unspecified amount. The Whitesand Band alleges that since at least the first half of the twentieth century, Ontario Hydro has erected dams, generating stations, electrical power lines and other facilities within or affecting the band's traditional lands and that those facilities have caused damage to band members and the lands, including substantial flooding and erosion. The Whitesand Band also claims treaty rights to a share of the profits arising from the activities of these Ontario Hydro facilities, an entitlement to increases in annuity payments established by treaty and for breach of an alleged contract to reimburse the Band for negotiation costs with Ontario Hydro. The Whitesand Band asserts multiple causes of action, including trespass, breach of fiduciary duty, nuisance and negligence. The May 24, 2001 case was consolidated in 2004 with a similar claim by Red Rock First Nation Band which commenced on September 7, 2001, as all procedural issues in both matters were the same. There is now one action in which the claims of both Whitesand and Red Rock are set out. The claims relating to activities of Ontario Hydro (i.e., flooding) are matters for which Ontario Power Generation Inc. would have responsibility pursuant to transfer orders under the *Electricity Act, 1998*. In the consolidated claim, Whitesand and Red Rock seek to tie Hydro One into the flooding allegations on the alleged basis of the integrated nature of the transmission system with the entire electricity system, which includes the method of generating power. To date, Hydro One has not filed a defence. Hydro One believes that it is unlikely that the outcome of this litigation will have a material adverse effect on its business, results of operations, financial position or prospects.

Health and Safety

Hydro One considers health and safety to be of paramount importance in the operation of its business and continues to maintain top quartile performance in key areas as well as to develop, implement and maintain progressive programs and initiatives. We are committed to creating and maintaining an injury-free workplace with concentrated focus on the elimination of serious injuries or "near-misses" which have the potential to cause serious injuries. We are developing a number of programs and initiatives for accident prevention and to minimize the risk of injury to the public associated with our facilities and operations. Policies are in place for both employee health and safety and public safety.

Corporate safety performance indicators and targets have been developed to measure serious incidents, especially those involving high energy levels that have the potential to cause fatalities and very serious injuries. In addition, measures are in place to monitor the days lost as a result of a workplace injury. These indicators are monitored by management and by the Health and Safety Committee of the Board of Directors. Management compensation is tied, in part, to success in achieving annual safety performance targets. An effective early and safe return to work process has allowed us to ensure that, when injuries occur, employees recover and return to the workplace as soon as possible.

Several programs and practices have been implemented to improve our safety performance. Actions currently underway include training programs and support for young workers, including apprentices, preserving core competencies through supervisory selection and reviewing/updating supervisory programs, improving the contracting process so as to ensure clear and consistent

standards for work performance, and better understanding of the human decision-making process to improve performance. Work site inspections and a safety rotation/mentoring program involving the major lines of business are also contributing to a safer workplace by identifying hazards, ensuring that proper barriers are in place before work is undertaken, as well as supporting the development and maintenance of a strong safety culture. Our incident investigation process allows us to learn as much as possible from incidents in order to develop improvements to job planning and prevent recurrences. A new Incident and Claims Management tool has been implemented.

Hydro One has integrated the management of health and safety into a single health, safety and environment management system. Effective risk assessment and management are key elements to the successful minimization of risk and safety performance improvement. Within the organization, hazards and risks have been identified and assessed and controls have been implemented to mitigate significant risks.

The Auditor General of Ontario

The mandate of the Office of the Auditor General of Ontario ("AG") was expanded to include conducting audits of entities such as Hydro One as a result of amendments to Ontario's *Auditor General Act* which came into effect on November 11, 2004. The 2006 Annual Report of the Office of the Auditor General of Ontario (the "Report") was tabled in the Legislative Assembly of Ontario on December 5, 2006. Section 3.07 of the Report contains the results of the first value-for-money audit conducted at Hydro One under the AG's expanded mandate. All of the AG recommendations in that Report have been implemented by our company and both the recommendations and actions taken are summarized in Chapter 4, Section 4.07 of the 2008 Annual Report of the Office of the Auditor General of Ontario tabled in the Legislative Assembly of Ontario on December 8, 2008 (the "Follow-up Report"). The Follow-up Report concluded that "Information we obtained from Hydro One suggests substantial progress was made in addressing all of the recommendations in our 2006 Annual Report".

REGULATION

The Statutory and Operating Framework

General

The *Electricity Act, 1998* and the *Ontario Energy Board Act, 1998*, as amended from time to time, primarily establish the broad legislative framework for Ontario's electricity market. The *Electricity Act, 1998* implemented the fundamental principles of the restructuring of Ontario's electricity industry, enabling the implementation of open non-discriminatory access to transmission and distribution systems. The *Ontario Energy Board Act, 1998* expanded the jurisdiction and mandate of the OEB to include regulation of the electricity and natural gas markets. Both statutes have been amended several times.[3]

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[3] Amending statutes include: *Reliable Energy and Consumer Protection Act, 2002 Electricity Pricing, Conservation and Supply Act, 2002, Ontario Energy Board Amendment Act (Electricity Pricing), 2003, Electricity Restructuring Act, 2004* and *Ontario Energy Board Consumer Protection and Governance Act, 2003* and the *Energy Conservation Responsibility Act, 2006.*

The OEB provides a framework for the review of electric distribution utilities' revenue requirements so that rates may be re-established based on this historical average or forecasted needs. See "Regulation – Rate Orders and Related Issues for Hydro One's Businesses – Distribution – Current Rate Orders and Distribution Rate Structure" and "Regulation – Rate Orders and Related Issues for Hydro One's Businesses – Distribution – Rate Orders for Remote Communities." Cost allocation issues are being addressed on an ongoing basis by a working group established by the OEB.

On March 28, 2006 the *Energy Conservation Responsibility Act, 2006* received Royal Assent. This legislation provides the framework for the installation of smart meters in all Ontario homes and small businesses by the end of 2010. Under the legislation, a new entity will oversee the communications systems and technologies, collect and manage data, and may facilitate meter procurement. Distributors will own, install, operate and maintain the meters. See "General Development of the Business – Smart Meters."

Contractual Arrangements, Codes and Licences

Operating Agreement with the IESO

Under the *Electricity Act, 1998*, the IESO is required to enter into agreements with transmitters giving it the authority to direct the operations of the transmitters' systems. On June 8, 2001, we signed our 10 year operating agreement with the IESO, which sets out the specific responsibilities of both parties relating to the provision of transmission service.

By contrast, the distribution portion of Ontario's network is not directed by the IESO and remains subject to the operational control of local distribution companies in accordance with the regulatory framework.

Hydro One's Relationships with Other Market Participants

Generators, local distribution companies and customers directly connected to our transmission system must enter into agreements with us to ensure reliable connection service in conformity with the Transmission System Code established by the OEB.

Some market participants, such as generators and large load customers embedded within distribution systems, are connected to the wholesale market through lines and facilities that are defined or deemed by the OEB as "distribution" and owned by local distribution companies. At a minimum, under the *Electricity Act, 1998*, local distribution companies must provide non discriminatory access for eligible generators and customers to the wholesale markets administered by the IESO. The local distribution companies must advise the IESO of any conditions in their distribution system that may affect the ability of embedded generators and loads to participate in the broader IESO administered markets.

Electricity Industry Codes

The OEB has issued and in some cases amended several Codes that govern the operation of OEB-licensed entities in Ontario. These Codes include the Affiliate Relationships Code for Electricity Distributors and Transmitters, the Standard Supply Service Code, the Transmission System Code, the Distribution System Code, the Retail Settlement Code, the Electricity Retailer

Code of Conduct, and most recently (issued in July 2008) the Smart Sub-Metering Code. These Codes and requirements prescribe minimum standards of conduct and standards of service for transmitters, distributors, smart sub-metering providers and/or retailers in the electricity market. These Codes are available on the OEB website at www.oeb.gov.on.ca.

Electricity Industry Licences

During 2003, the OEB undertook a review of the licences of all electricity transmitters, distributors and generators in Ontario. The new licences have a 20-year term and incorporate the reporting and record-keeping requirements in accordance with the OEB's Electricity Reporting and Record Keeping Requirements. New licences for all of our regulated businesses were issued in 2003 and 2004.

Transmission Licence

The following are the key conditions of our transmission licence:

- ***Obligation to Enter into Agreement with the IESO*** – We are required to enter into the operating agreement with the IESO, providing for the IESO's direction of the operation of our transmission system. On June 8, 2001, we signed our operating agreement with the IESO. See "Regulation – Contractual Arrangements, Codes and Licences – Operating Agreement with the IESO."

- ***Non-discriminatory Access*** – If a generator, distributor, retailer, wholesaler or customer requests that we convey electricity using our transmission system, subject to capacity constraints, we must make an offer to convey electricity on behalf of the applicant consistent with the applicable Market Rules and the Transmission System Code.

- ***Obligation to Connect*** – We may not refuse an offer to connect to our transmission system which has been made in accordance with the terms of our transmission rate order, the Market Rules and the Transmission System Code unless we are permitted to do so by the OEB, the legislation or any codes, standards or rules with which we are obligated to comply as a condition of our licence. We must respond to a request for connection within 30 business days in compliance with published connection procedures.

- ***Obligation to Maintain System Integrity*** – We must maintain our transmission system to the standards established in our agreement with the IESO, the Market Rules and any other recognized industry operating or planning standard which has been specified by the OEB.

- ***Transmission Rates*** – We may not impose charges for the transmission of electricity or connection to our transmission system except in accordance with our transmission rate order.

- ***Separation of Business Activity*** – Our transmission business must separate its financial records from those of any other business of Hydro One.

- ***Expansion of the Transmission System*** – Construction, expansion or reinforcement of our transmission system is subject to legislation, regulatory approvals, licences, codes and the Market Rules. Either the IESO or the OEB may require us to expand or reinforce our transmission system if it determines that doing so is necessary for the maintenance of security, reliability or integrity of the system. See "Description of the Business – Our Transmission Business – Projects Relating to Interconnection Capacity."

- ***Information Disclosure*** – We are required to maintain records, provide the OEB with information it may require from time to time and inform the OEB of any material change in circumstances no more than 20 days after the date of occurrence.

- ***Restrictions on Provision of Information*** – We are restricted in our use and disclosure of information pertaining to consumers, retailers, wholesalers and generators. We must obtain consent for disclosure of such information, except in certain specified situations and inform such parties of the conditions under which their information may be disclosed without their consent.

Distribution Licences

The terms and conditions of our three distribution licences are similar to the terms and conditions of our transmission licence described above. In addition, these licences:

- ***Separation of Business Activity*** – require the distribution business to keep its financial records separate from those of the transmission business;

- ***Distribution Rates*** – create an obligation to charge rates in accordance with an order of the OEB and in accordance with the methods or techniques set out in the Electricity Distribution Rate Handbook, the Distribution System Code, the Standard Supply Service Code and the Retail Settlement Code;

- ***Code Compliance*** – require compliance with the Retail Settlement Code and the Affiliate Relationships Code for Electricity Distributors and Transmitters;

- ***Commodity Rebates*** – prescribe the manner by which we must pass through any rebates from OPG to customers; and

- ***Obligation to Connect and Serve*** – impose the obligation on our distribution business to connect a building to our distribution system under prescribed circumstances, and to sell electricity or ensure electricity is supplied to every person connected to our distribution system, in accordance with our distribution rate orders and the Standard Supply Service Code, and to sell electricity to consumers consistent with the terms and conditions of these instruments.

Hydro One Networks Inc. holds an interim Distribution Licence to serve the community of Cat Lake in Northwestern Ontario. The interim licence was first issued in July 2006 and has been renewed on several occasions for sequential terms of three months each.

Rate Orders and Related Issues for Hydro One's Businesses

The OEB approves both the revenue requirements of and the rates charged by our regulated businesses. The rates are designed to permit our businesses to recover the allowed costs and to earn a specified annual rate of return on our common equity.

The term "utility rate base" refers to the investment in regulated operations (consisting of gross plant in service, less accumulated depreciation, plus necessary working capital and excluding construction work in process). Utility rate base is used to determine the capital structure for our regulated businesses, enabling a determination of approved financing charges and return on common equity for them.

Transmission

Current Rate Orders and Review of the Existing Transmission Rate Structure

On October 26, 2005, the OEB initiated a proceeding to review our transmission rates and to approve revenue requirements for 2006, 2007, and 2008.

On November 23, 2005, we proposed to the OEB an earnings-sharing mechanism that would result in excess or deficient earnings being tracked. On February 21, 2006, the OEB adopted an earnings-sharing mechanism to equally share, between our shareholder and customers, any transmission earnings in excess of the approved rate of return of 9.88% for the period January 1, 2006 until new rates were set. Consequently, 50% of our excess earnings recovered from customers were deferred as a regulatory liability. This decision had the effect of reducing our transmission revenues by $33 million in 2006.

A decision on Hydro One Networks Inc.'s 2007 and 2008 Transmission Revenue Requirement and Rate Application was delivered on August 16, 2007, which approved:

- Hydro One's Capital and Operations, Maintenance & Administration ("OM&A") expenditures for 2007 and 2008 as requested.
- A deemed regulatory capital structure of 60% debt and 40% equity. The deemed capital structure was the same as previously approved for Hydro One's distribution business.
- A Return on Equity ("ROE") set at 8.35%, as compared to the requested 10% in 2007 and 10.25% in 2008. The OEB's view was that there was no meaningful difference in risk between distribution and transmission, and accordingly approved an ROE using the same methodology applicable to electricity distributors.
- Expensing the carrying costs associated with the Niagara Reinforcement Project, a $97 million investment that is being prevented from being put into service and added to rate base due to reasons beyond Hydro One's control.
- Refunding the customer's portion of the 2006 earnings-sharing and the revenue collected under current rates in excess of our revenue requirement for the period from January 1, 2007 to October 31, 2007 (Revenue Difference Deferral Account - RDDA). These revenues were refunded to customers over the fourteen month period from November 1, 2007 to December 31, 2008, which is the effective period for the new Uniform Transmission Rates approved by the OEB, as discussed below.

On September 28, 2007 the OEB issued its final order approving Hydro One's revenue requirements of $1,156 million and $1,170 million, for 2007 and 2008 respectively, total deferral account recovery of -$36.5 million (including -$28.4 million of earnings-sharing refund) in each of 2007 and 2008, and an RDDA amount of -$85.3 million.

As part of a joint proceeding involving all transmitters in Ontario, on October 17, 2007 the OEB issued a rate order approving new Ontario Uniform Transmission Rates for implementation on November 1, 2007 through to December 31, 2008. The new Uniform Transmission Rates were, on average, 12% lower than previously approved rates and resulted in approximately a 1% decrease in the average customer's total electricity bill.

On August 28, 2008 the OEB approved an adjustment to the Uniform Transmission Rates which allows Hydro One to recover revenues consistent with the Board-approved 2008 revenue requirement, commencing January 1, 2009. This adjustment provides for a 9.2% increase from the 2008 transmission rates, resulting in an approximately 1% total bill impact for the typical customer.

Uniform Transmission Rates are based on the fully allocated cost associated with providing each of the following three transmission service elements:

- ***Network services*** — the transmission network is the integrated part of our high voltage transmission system that is shared by all users and includes all 500 kV facilities, the 230 kV and the 115 kV facilities that can be classified as commonly used;

- ***Line connection services*** — connection facilities are the radial parts of our high voltage transmission system, which are dedicated to serving a single customer or generator or a group of customers or generators. Transmission line connection facilities are the radial high voltage transmission lines connecting the transformer to the network; and

- ***Transformation connection services*** — the transformation connection assets consist of the high voltage transformation facilities that step down voltages from transmission levels to distribution levels to supply customers.

In addition, electricity exports from Ontario are levied an export charge for transmission of one dollar per MWh.

Hydro One Networks filed its 2009 – 2010 Transmission Revenue Requirement and Rate Application with the OEB on September 30, 2008. The requested revenue requirement is $1,233M in 2009 and $1,341M in 2010. If approved, this will result in 6.4% and 12.1% year–over-year increases in transmission rates for 2009 and 2010, respectively, as compared to the Uniform Transmission Rates effective as of January 1, 2009 set in August 2008. These, in turn, represent estimated increases on total customer bills of 0.5% in 2009 and 0.9% in 2010. The oral hearing was held in February 2009 and a decision is expected by the summer of 2009.

Competition

Under the *Ontario Energy Board Act, 1998*, any licensed competitor can apply to the OEB for approval to build transmission network facilities in Ontario. The OEB's adoption of the Uniform Transmission Rate reduces the financial incentive for customers to seek alternative transmission.

Customers historically had the option to build and own their own transmission connection facilities and thereby avoid paying our connection charge. Only a few large industrial customers and local distribution companies chose to do so, likely because of the significant costs of construction. Under the new regulatory framework, in addition to avoiding our connection charge, local distribution companies that own their transmission connection facilities can include these assets in their rate base and earn a regulated return. Customers will generally, however, continue to have the option to have their new connection facilities incorporated within our existing transmission transformation and line pools or to build and own their new connection facility. We expect to continue to maintain and restore our existing connection assets, as well as bid on the construction and ownership of new facilities.

By-pass

By-pass occurs when we have invested in the provision of transmission facilities to a customer which then obtains all or part of its transmission services in another manner or takes action to avoid its use of transmission services before the rates collected have paid for the investment. Recovery of the remaining costs for the stranded facilities then necessitates higher transmission rates from the remaining customers.

In its January 2001 decision respecting transmission rate design and cost allocation, the OEB addressed the issue of by-pass where a load customer installs a generator to serve all or part of its load. The OEB decided that customers would be assessed line and transformation connection charges based on their total demand for electricity, or gross load. However, given the desire to encourage new generation and the growth anticipated in the usage of the network (which would hold us harmless from the effects of stranding), customers would be assessed network charges based on their net load. In effect, customers who generate electricity on-site can save the network charges otherwise applicable to their purchase of electricity generated by third parties. The decision to assess line and transformation connection charges based on gross loads means that on-site generators bear a portion of the costs associated with Ontario's transmission infrastructure, thereby mitigating the potentially negative effect of on-site generation on our transmission business.

In August, 2005, following an extensive consultation process, the OEB issued a revised Transmission System Code, which implements its June 2004 decision on principles relating to transmission by-pass, among other things. See "Regulation – Contractual Arrangements, Codes and Licences – Electricity Industry Codes."

Facilities Applications

Transmission line expansions greater than 2 kilometres in length require prior OEB approval under section 92 of the *Ontario Energy Board Act, 1998*, as well as environmental assessment

and other approvals. On November 14, 2006, the OEB issued filing requirements for transmission applications which include filing requirements for leave to construct electricity transmission projects under section 92 of the *Ontario Energy Board Act, 1998*. These requirements are used to ensure a complete review of proposed transmission projects.

On August 29, 2007, the OPA filed its first IPSP with the OEB for approval. In its application, the OPA did not seek to prove the need for any transmission projects included in the IPSP, which would have avoided the requirement to have project need approved for those projects in a subsequent OEB leave-to-construct proceeding. As a result, transmitters will be required to submit a full leave-to-construct application, including for project need, when applying to the OEB for leave to construct these transmission projects. Regardless of whether OEB leave to construct is received, cost recovery of approved facilities still needs a final approval from the OEB as part of a transmission rate application.

On Sept. 17, 2008 the Minister of Energy and Infrastructure issued a supplemental directive directing the OPA to revisit the current IPSP in order to accelerate conservation targets and increase the amount of renewable energy sources in the supply mix. Additionally, the Minister asked the OPA to undertake an enhanced process of consultation with First Nations and Metis communities in light of potential duty to consult obligations. As a result of the directive and the tabling of the proposed Green Energy Act, the OPA has indicated that it expects to be able to file a revised IPSP sometime in the summer of 2009, subject to passage of the Green Energy Act.

Connection Cost Responsibility and Enabler Lines

In January 2008, the OEB initiated a consultation process to examine the issue of cost responsibility associated with the connection of generation and load facilities to electricity transmission systems. The OEB decided to examine its cost responsibility policies at this time for several reasons, including the large number of connections that are expected to be required for generation facilities using renewable sources of energy.

On October 29, 2008, the OEB issued its proposal to amend the Transmission System Code, adopting a "hybrid" option for cost responsibility for enabler lines required by an approved IPSP or driven by a Minister's directive. The hybrid option would see initial pooling of the costs of enabler lines by the transmitter, with generators paying their pro-rata share when ready to connect. The proposal includes a process for designating transmitters to develop and construct such facilities. Stakeholder comments on the proposal were due on December 1, 2008.

Transmission Corridors

On June 27, 2002, the Province passed the *Reliable Energy and Consumer Protection Act, 2002* that provided for, among other things, ownership of all transmission corridor and abutting lands to be transferred from us to the Province in exchange for a statutory right to use the lands for transmission and distribution purposes effective December 31, 2002. Certain of these lands have been subsequently transferred back to Hydro One. See "Interests of Management and Others in Material Transactions – Relationship with Province and Other Parties – Transmission Corridors."

Distribution

Current Rate Orders and Distribution Rate Structure

On April 26, 2005, Hydro One received OEB approval for a rate amendment affecting embedded customers connected to the Hydro One low voltage distribution system that are supplied from multiple delivery points at a single transformation station and who pay retail transmission charges. The amendment allows the aggregation of demand for such customers and is intended to align the basis on which they are charged retail transmission rates with that employed by the IESO in charging transmission rates to wholesale transmission customers supplied from multiple delivery points at a single transformation station. The reduction in charges to customers will be recovered through the retail settlement variance accounts.

On August 17, 2005, Hydro One filed a Distribution Rate Application seeking approval for a $160 million increase in the 2006 revenue requirement for our distribution business to a total of $965 million. An oral hearing commenced in January 2006. On April 12, 2006 the OEB granted full approval of the $965 million revenue requirement. The return on equity for our distribution business was approved at 9.0%. New rates added approximately 4.8% ($6.53 per month) to our typical residential customers' total bill (based upon usage of 1,000 kWh per month). The new rates came into effect on May 1, 2006.

In January 2007, Hydro One Brampton Networks Inc. submitted a rate application to the OEB for rates that became effective in May, 2007. This rate application increased distribution rates by 0.49%. The OEB approved the application on April 12, 2007. In addition, Hydro One Brampton Networks Inc. requested and received an increase to the Smart Metering rate rider from $0.28 cents per metered customer per month to $0.67 cents per metered customer per month. The overall impact of the decision on a typical residential customer's total bill (based upon usage of 1,000 kWh per month), after reductions to the RPP were factored in, is expected to be a decrease of approximately 0.3%.

On February 19, 2007 Hydro One Networks Inc. applied for a 2007 distribution rate increase. The OEB approved a rate increase of 0.457% to Hydro One's distribution rates for 2007 commencing May 1, 2007, which factored in a 1.92% price escalation factor, less a productivity gain of 1%, less the impact of the elimination of the large corporation tax. Hydro One also sought, and was granted approval for, an increase in the rate rider for the implementation of smart meter infrastructure from $0.27 per metered customer to $0.93 per metered customer commencing May 1, 2007.

On August 15, 2007 Hydro One Networks Inc. filed the revenue requirement portion of its 2008 cost of service application in accordance with the OEB's multi-year distribution rate-setting plan. Hydro One sought approval of a revenue requirement of $1,067 million for the 2008 test year. The resulting distribution rate increase for the average customer was forecast to be less than 2.5%, on average, over approved 2007 distribution rates as a result of the requested revenue requirement, expiry of historical rate riders to recover costs associated with a prior period, the expiry of interim costs for smart meters, and the recovery of regulatory assets. The requested distribution rate increase amounted to an average increase of less than 1% on the average customer total bill.

On December 18, 2007, Hydro One filed the details on its cost allocation and rate design proposals, which included a plan to reduce the number of rate classes for its customers and

consolidate, or harmonize, the rates for its existing rate classes to the new proposed rate classes. An oral hearing was held in July 2008.

On December 18, 2008, the OEB issued its decision on our distribution rates application, which approved:

a) the requested rate harmonization plan, reducing the existing 280 rate classes to 12 over a period of four years;
b)a 2008 OM&A budget of $466 million;
c) a 2008 capital budget of $401 million; and
d) 2008 capital expenditures of $165 million and OM&A expenditures of $10 million for smart meters that will continue to be recorded in a deferral account.

The net effect of the decision is a reduction in our revenue requirement from $1,067 million requested to about $1,028 million. New rates were approved effective as of May 1, 2008 and were implemented February 1, 2009, resulting in the retroactive recovery of the approved revenue requirement over 27 months commencing February 1, 2009 through April 30, 2011. Approximately $25 million of incremental revenue was recorded for accounting purposes in December 2008.

On August 2, 2007 the OEB initiated a consultation on the development of the principles and methodology for a 3rd generation incentive regulation mechanism. This consultative process culminated with the issuance of an OEB report on July 14, 2008 and a supplemental report on September 17, 2008 that will be used to adjust electricity distribution rates starting in 2009 for those utilities whose 2008 rates were rebased.

On November 7, 2008 Hydro One filed its 3rd Generation Incentive Regulation Mechanism application to the OEB for 2009 Distribution rates. On January 30, 2009 Hydro One submitted an update to its application to reflect the OEB December 18, 2008 revenue requirement decision and the associated January 28, 2009 approved rate order. Applying the OEB-specified methodology, Hydro One's application proposes an increase of approximately 4% effective May 1st, 2009. The proposed 4% increase comprises a 1% price cap index on basic rates and rate riders (equivalent to a 3% increase) to recover incremental revenue requirements on a portion of proposed capital expenditures and forecasted 2009 smart meter costs.

Rate Orders for Hydro One Remote Communities Inc.

Hydro One Remote Communities Inc.'s business is exempt from a number of sections of the *Electricity Act, 1998* which relate to the competitive market. For example, we continue to apply bundled rates to customers in remote communities. In accordance with the OEB's Multi-Year Electricity Distribution Rate Setting Plan, Hydro One Remote Communities Inc. filed a Rate Application on August 29, 2008. This application was subsequently updated in late November, 2008 to reflect a significant change in diesel fuel costs over the intervening period. Increases to both customer rates and the required level of Rural and Remote Electricity Rate Protection ("RRRP") funding are requested due primarily to increases in diesel fuel costs occurring since the prior rates approval in 2006. Specifically, the application seeks to recover a revenue requirement of $42.5 million and to establish the RRRP in 2009 at $31.9M. The previous RRRP amount collected from Ontario grid customers on behalf of Hydro One Remote Communities

Inc. was $21.1 million. The proposed average increase for Hydro One Remote Communities Inc.'s customers is 4.4%. Interrogatories were received from OEB staff and intervenors by mid-December and Hydro One's replies were submitted in mid-January.

Rural and Remote Rate Protection

In approving electricity rates for a distributor which delivers electricity to rural or remote consumers, the OEB is required to provide rate protection for prescribed classes of consumers, including those who received rural rate assistance prior to April 1, 1999, by reducing the rates that would otherwise apply.

Since January 1, 2003, the amount of rate reduction for our rural consumers who occupy rural residential premises is $127 million per year less the specific amounts established for distributors in three former remote communities.

In 2007, our remote customers received a rate reduction in the amount of $21.1 million. This amount was set by the OEB according to the rules set out in the regulations under the *Ontario Energy Board Act, 1998*.

Under the *Ontario Energy Board Act, 1998*, a distributor is entitled to be compensated for lost revenue resulting from the rate protection regime, and all consumers are required to contribute towards the amount of any compensation to the distributors, such as our company, for rate protection. As of May 1, 2002, the amounts required to compensate the distributors were collected by the IESO and paid to us for distribution in accordance with the regulation under the *Ontario Energy Board Act, 1998*. The OEB calculates the charge to be collected by the IESO based upon the latter's forecast of the number of kilowatt-hours of electricity that will be withdrawn from the IESO-controlled grid. Hydro One Networks Inc. maintains a variance account to track any surplus or deficit in the amount received from the IESO and from the $127 million prescribed amount.

Hydro One Remote Communities Inc.'s business is run on a break even basis. As a result, any net earnings or loss in the year, including rural and remote rate protection amounts, is deferred in a regulatory variance account for inclusion in the calculation of future customer rates.

Competition

Under the *Ontario Energy Board Act, 1998*, there are instances in which it is appropriate for one distributor to transfer its customers to another distributor. The acquiring distributor is required to obtain amendments to its licence authorizing it to serve in a specific area, but not with exclusive distribution rights to it. On February 27, 2004, the OEB issued its decision, with clear principles and filing requirements to be followed for service territory amendment applications.

In July 2005, as a result of three applications by distributors, a generic proceeding was convened by the OEB to determine issues relevant to inter-utility share acquisitions and amalgamations. In a decision issued on August 31, 2005, the OEB decided that the scope of its review of these applications is appropriately dictated by Section 86 of the *Ontario Energy Board Act, 1998* and its objectives as stated. It also decided that reviews of the related transaction processes themselves were beyond its purview.

RISK FACTORS

Ownership by the Province

The Province owns all of our outstanding shares. Accordingly, the Province has the power to determine the composition of our Board of Directors and appoint the Chair, and thus influence our major business and corporate decisions. We and the Province have entered into a memorandum of agreement relating to certain aspects of the governance of our company. Pursuant to such agreement, in September 2008 the Province made a declaration removing certain powers from the directors of Hydro One pertaining to the off-shoring of jobs under the outsourcing arrangement with Inergi LP. See "Interest of Management and Others in Material Transactions – Relationships with the Province and Other Parties – Memorandum of Agreement". The Province may make similar declarations in the future, some of which may have an adverse effect on our business. Conflicts of interest may arise between us and the Province as a result of the obligation of the Province to act in the best interests of the residents of Ontario in a broad range of matters, including the regulation of Ontario's electricity industry and environmental matters, any future sale or other transaction by the Province with respect to its ownership interest in our company, the Province's ownership of OPG, and the determination of the amount of dividend or proxy tax payments. We may not be able to resolve any potential conflict with the Province on terms satisfactory to us which would have an adverse impact on our business.

Risk Associated with Transmission Projects

The amount of power which may flow through transmission networks is constrained due to the physical characteristics of transmission lines and operating limitations. Within Ontario, new and expected generation expansions and load growth have increased such that parts of Hydro One's transmission and distribution systems are operating at or near capacity. These constraints or bottlenecks limit the ability of Hydro One's networks to reliably transmit power from new and existing generation sources (including, expanded interconnections with neighbouring utilities) to load centres or meet customers' increasing loads. As a result, investments have been initiated to increase transmission capacity and enable the reliable delivery of power from existing and future generation sources to Ontario consumers.

In many cases, these investments are contingent upon one or more of the following approvals or processes: (a) environmental approval(s), (b) receipt of OEB approvals which can include expropriation and (c) appropriate consultation processes, and where appropriate, accommodation with First Nations and Métis who may be potentially affected by a project. Obtaining these approvals and carrying out these processes may also be impacted by public opposition to the proposed site of transmission investments, thus there is a risk that necessary approvals may not be obtained in a timely fashion or at all. This will adversely affect transmission reliability and/or our service quality.

Work Force Demographic Risk

By the end of 2008, more than 20% of Hydro One's employees were eligible for retirement and by 2010 there may be more than 40% eligible to retire. Accordingly, our success will be tied to our ability to attract and retain sufficient qualified staff to replace those retiring. This will be challenging as we expect the skilled labour market for our industry to be highly competitive in

the future. In addition, many of our employees possess experience and skills that will also be highly sought after by other organizations both inside and outside the electricity sector. We have already lost a considerable number of management staff, both those in executive positions and those who are logical successors for executive positions, to opportunities in other electricity sector positions across Canada (and, in particular, in Ontario) as well as senior positions outside of the sector. Moreover, we must also continue to advance our training and apprenticeship programs and succession plans to ensure that our future operational staffing needs will be met. If we are unable to attract and retain qualified personnel, it could have a material adverse effect on our business.

Asset Condition

Hydro One continually monitors the condition of its assets and maintains, refurbishes or replaces them to maintain equipment performance and provide reliable service quality. Capital and maintenance programs have been increased to maintain the performance of our aging asset base. Execution of these plans is dependent on external factors, however, including the fact that opportunities to remove equipment from service to accommodate construction and maintenance are becoming increasingly limited due to customer and generator priorities. Lead times for material and equipment have also increased substantially due to increased demand and limited vendor capability.

If we are unable to carry out these plans, in a timely and optimal manner, equipment performance will degrade which may compromise the reliability of the provincial grid, our ability to deliver sufficient electricity and/or customer supply security and increase the costs of operating and maintaining these assets. This could have an adverse impact on our company.

Regulatory Risk

We are subject to regulatory risks, including the approval by the OEB of rates for our transmission and distribution businesses that permit a reasonable opportunity to recover the estimated costs of providing service on a timely basis and earn the approved rates of return.

The OEB approves our transmission and distribution rates based on projected electricity load and consumption levels. If actual load or consumption falls below projected levels, our rate of return for either, or both, of these businesses could be adversely affected. Also, our current revenue requirements for these businesses are based on cost assumptions that may not materialize. There is no assurance that the OEB would allow rate increases sufficient to offset unfavourable financial impacts from unanticipated changes in electricity demand or in our costs.

Our load could also be negatively impacted by successful CDM programs. Current requirements for CDM call for a 5% reduction in Ontario's projected peak electricity demand by 2010. These expectations are factored into our revenue requirements for OEB approval, to ensure that the targeted CDM accomplishments do not result in deteriorated revenues. There is a risk that our revenues would be reduced if these targets are exceeded. The OEB has recognized the need to compensate utilities for such lost revenue, but the approach, level and timing of any such compensation mechanism is yet to be determined. We are also subject to risk of revenue loss from other factors.

As a transmitter, we expect to make significant investment in the coming years in large-scale transmission infrastructure projects, and to connect new third-party load and generation assets. Additionally, there is always the possibility that we could incur unexpected capital expenditures to maintain or improve our assets. The risk exists that the OEB may not allow full recovery of such investments. To the extent possible, we try to mitigate this risk by seeking from the regulator clear policy direction on cost responsibility, and pre-approval of the need for capital expenditures.

The Province has passed regulations authorizing us, as a distributor, to procure smart meters but we are only currently authorized to recover $0.93 per metered customer per month of the associated costs in rates ($0.67 in the case of Hydro One Brampton Networks Inc.).

While we expect all of our expenditures to be fully recoverable after OEB review, any future regulatory decision to disallow or limit the recovery of such costs would lead to potential impairment and charges to operations.

Market and Credit Risk

Market risk refers primarily to the risk of loss that results from changes in commodity prices, foreign exchange rates and interest rates. We do not have commodity risk. We do have foreign exchange risk as we enter into agreements to purchase materials and equipment associated with our capital programs and projects that are settled in foreign currencies. This foreign exchange risk is not material. We could in the future decide to issue foreign currency denominated debt which, however, we would expect to hedge back to Canadian dollars, consistent with our company's risk management policy. We are exposed to fluctuations in interest rates as our regulated Return on Equity (ROE) is derived using a formulaic approach which is in part based on the forecast for long-term Government of Canada bond yields. We estimate that a one percent decrease in the forecast long-term Government of Canada bond yield used in determining our ROE would reduce our transmission business net income by approximately $21 million and our distribution business net income by approximately $13 million. Our net income is adversely impacted by rising interest rates as our maturing long-term debt is refinanced at market rates. We periodically utilize interest rate swap agreements to mitigate elements of interest rate risk.

Financial assets create a risk that a counter-party will fail to discharge an obligation, causing a financial loss. Derivative financial instruments result in exposure to credit risk, since there is a risk of counter-party default. We monitor and minimize credit risk through various techniques, including dealing with highly-rated counter-parties, limiting total exposure levels with individual counter-parties, and by entering into master agreements which enable net settlement. We do not trade in any energy derivatives. We do, however, have interest rate swap contracts outstanding from time to time. Currently, there are no significant concentrations of credit risk with respect to any class of financial assets. We are required to procure electricity on behalf of competitive retailers and embedded local distribution companies for resale to their customers. The resulting concentrations of credit risk are mitigated through the use of various security arrangements, including letters of credit, which are incorporated into our service agreements with these retailers in accordance with the OEB's Retail Settlements Code.

Risk Associated with Arranging Debt Financing

We expect to borrow to repay our existing indebtedness and fund a portion of capital expenditures. We have substantial amounts of existing debt which mature between 2009 and 2012, including $400 million maturing in 2009 and $600 million maturing in 2010. We also plan to incur total capital expenditures in excess of $1.6 billion in 2009 and capital expenditures are expected to exceed $1.7 billion in 2010. Cash generated from operations, after the payment of expected dividends, will not be sufficient to fund the repayment of our existing indebtedness and capital expenditures. Our ability to arrange sufficient and cost effective debt financing could be adversely affected by numerous factors, including the regulatory environment in Ontario, our results of operations and financial position, market conditions, the ratings assigned to our debt securities by credit rating agencies and general economic conditions. Any failure or inability on our part to borrow substantial amounts of debt on satisfactory terms could impair our ability to repay maturing debt, fund capital expenditures and meet other obligations and requirements and, as a result, could have a material adverse effect on our company.

Pension Plan Risk

We have a defined benefit registered pension plan for the majority of our employees. Contributions to the pension plan are established by actuarial valuations which are filed with the Financial Services Commission of Ontario on a tri-annual basis. The most recently filed valuation was prepared as at December 31, 2006 and was filed in September 2007. The next valuation is required to be prepared as at December 31, 2009. Contributions beyond 2009 will be based on an actuarial valuation effective December 31, 2009 and will depend on future investment returns, changes in benefits or actuarial assumptions. As a result of the current economic uncertainty and financial market volatility, our pension plan experienced negative returns in 2008 of approximately 22.5%. Should our plan continue to incur negative returns in 2009 or fail to recover a substantial portion of the losses incurred in 2008, or if the discount rate falls sufficiently by the end of 2009, the deficit position at that time could lead to a large increase in our contribution requirements beyond 2009. A determination by the OEB that some of our pension expenditures are not recoverable from customers would have a negative impact on our company.

Risk of Natural and Other Unexpected Occurrences

Our facilities are exposed to the effects of severe weather conditions, natural disasters and, potentially, catastrophic events, such as a major accident or incident at a facility of a third party (such as a generating plant) to which our transmission or distribution assets are connected. Although constructed, operated and maintained to industry standards, our facilities may not withstand occurrences of this type in all circumstances. We do not have insurance for damage to our transmission and distribution wires, poles and towers located outside our transmission and distribution stations resulting from these events. Losses from lost revenues and repair costs could be substantial, especially for many of our facilities that are located in remote areas. We could also be subject to claims for damages caused by our failure to transmit or distribute electricity. Our risk is partly mitigated because our transmission system is designed and operated to withstand the loss of any major element and possess inherent redundancy (e.g. several interconnections with utilities in other provinces and the United States) that provides alternate means to deliver large amounts of power. In the event of a large uninsured loss we would apply to the OEB for recovery of such loss; however, there can be no assurance that the OEB would

approve any such applications, in whole or in part, which could have a material adverse effect on our net income.

Risk from Transfer of Assets Located on Indian Lands

The transfer orders by which we acquired certain of Ontario Hydro's businesses as of April 1, 1999 did not transfer title to some assets located on lands held for bands or bodies of Indians under the *Indian Act* (Canada). See "Interest of Management and Others in Material Transactions – Relationships with the Province and Other Parties – Transfer Orders." Currently, OEFC holds these assets. Under the terms of the transfer orders, we are required to manage these assets until we have obtained all consents necessary to complete the transfer of title of these assets to us. We cannot predict the aggregate amount that we may have to pay, either on an annual or one-time basis, to obtain the required consents. However, we anticipate having to pay more than the $717,000 that we paid to these Indian bands and bodies in 2008. If we cannot obtain consents from the Indian bands and bodies, OEFC will continue to hold these assets for an indefinite period of time. If we cannot reach a satisfactory settlement, we may have to relocate these assets from the Indian lands to other locations at a cost that could be substantial or, in a limited number of cases, to abandon a line and replace it with diesel generation facilities. The costs relating to these assets could have a material adverse effect on our net income if we are not able to recover them in future rate orders.

Risk Associated with Information Technology Infrastructure

Our ability to operate effectively in the Ontario electricity market is in part dependent upon us developing, maintaining and managing a complex information technology systems infrastructure. Computer systems are employed to operate our transmission and distribution facilities, financial and billing systems, and business systems to capture data and to produce timely and accurate information. We continue to transition most of our financial and business processes to an integrated business and financial reporting system. The conversion of these systems and processes may expose us to risk, including risks associated with maintaining internal controls, as the data and business processes are transitioned and new systems are brought online. We are also updating our transmission management system. Failures of our financial, business and operating systems could have a material adverse effect on our business, operating results, financial condition or prospects.

Environmental Risk

Our health, safety and environmental management system is designed to ensure hazards and risks are identified and assessed, and controls are implemented to mitigate significant risks. We cannot guarantee, however, that all such risks will be identified and mitigated without significant cost and expense to our company. The following are some of the areas that may have a significant impact on our operations.

We are subject to extensive Canadian federal, provincial and municipal environmental regulation. Failure to comply could subject us to fines and other penalties. In addition, the presence or release of hazardous or other substances could lead to claims by third parties and/or governmental orders requiring us to take specific actions such as investigating, controlling and remediating the effects of these substances. We are currently undertaking a voluntary land assessment and remediation program covering most of our stations and service centres. It

involves the systematic identification of any contamination at or from these facilities, and, where necessary, the development of remediation plans for our company and adjacent private properties. Any contamination on our properties could limit our ability to sell these assets in the future.

There is also risk associated with obtaining governmental approvals, permits, or renewals of existing approvals and permits related to constructing or operating facilities. This may require environmental assessment or result in the imposition of conditions, or both, which could mean delays and cost increases.

On September 17, 2008, Environment Canada published final regulations governing the management of PCBs. We recorded a liability based on our best estimate of the future expenditures required to comply with these regulations. Most of these additional expenditures are expected to be incurred in the 2013 to 2025 period. Actual future environmental expenditures may vary materially from the estimates used in the calculation of the environmental liabilities on our balance sheet. We do not have insurance coverage for these environmental expenditures.

Scientists and public health experts have been studying the possibility that exposure to electric and magnetic fields emanating from power lines and other electric sources may cause health problems. If it were to be concluded that electric and magnetic fields present a health risk, or governments decide to implement exposure limits, we could face litigation, be required to take costly mitigation measures such as relocating some of our facilities or experience difficulties in locating and building new facilities.

Labour Relations Risk

The substantial majority of our employees are represented by either the PWU or the Society. Over the past several years, significant effort has been expended to increase our flexibility to conduct operations in a more cost efficient manner. Although we believe that we have achieved improved flexibility in our collective agreements, including a reduction in pension benefits similar to a previous reduction affecting management staff, we may not be able to achieve further improvement. The existing collective agreement with the PWU will expire on March 31, 2011 and the existing Society collective agreement will expire on March 31, 2013. We face financial risks related to our ability to negotiate collective agreements consistent with our rate orders. In addition, in the event of a labour dispute, we could face some degree of operational risk related to continued compliance with our licence requirements of providing service to customers.

Risk Associated with Outsourcing Arrangement

Consistent with our strategy of reducing operating costs, we entered into an outsourcing services agreement in 2002 with Inergi LP, an affiliate of CapGemini Canada Inc. See "Description of the Business – Outsourcing Arrangement with Inergi LP." If the agreement with Inergi LP is terminated for any reason, we could be required to incur significant expenses to re-establish all or some of the functions involved, which could have a material adverse effect on our business, operating results, financial condition or prospects. The agreement expires on February 29, 2012. Given the complexities involved, we have begun developing a plan of action for end-of-term.

Risk from Provincial Ownership of Transmission Corridors

Pursuant to the *Reliable Energy and Consumer Protection Act, 2002*, the Province acquired ownership of our transmission corridor lands underlying our transmission system. Although we have the statutory right to use the transmission corridors, we may be limited in our ability to expand our systems. Also, other uses of the transmission corridors by third parties in conjunction with the operation of our systems may increase safety or environmental risks.

DIVIDENDS

Dividends on our common shares and Series A preferred shares are declared at the discretion of our Board of Directors, and are recommended by our management based on our results of operations, financial condition, cash requirements and other relevant factors, such as industry practice and shareholder expectations.

Our company's policy is to declare and pay cash dividends on our common shares on the basis of a calculation involving our regulated net income net of preferred dividends and non-regulated net income. Any factor that adversely affects our company's net income would likely be reflected in our dividend payments.

We declared and paid to the Province annual dividends on our outstanding 100,000 common shares totalling $241 million in 2008 as compared with $307 million in 2007 and $332 million in 2006. We declared and paid to the Province a total annual cumulative dividend on our outstanding 12,920,000 series A preferred shares of approximately $18 million in each of 2008, 2007, and 2006, which was calculated at a rate of $1.375 per annum per share, as stipulated in our company's Articles of Incorporation. In addition, we made payments in lieu of taxes to the Province in 2008 in the amount of approximately $145 million, as compared to $230 million in 2007.

DESCRIPTION OF CAPITAL STRUCTURE

General Description of Capital Structure

The authorized share capital of our company consists of an unlimited number of common shares (the voting shares of our company) and an unlimited number of preferred shares. As at December 31, 2008, 100,000 common shares and 12,920,000 series A preferred shares are issued and outstanding, all of which are owned directly by the Province.

All of our company's voting securities are held by the Province. Accordingly, our company is controlled by the Province.

The common shares are not redeemable or retractable. Holders of our common shares are entitled to one vote per share at meetings of the shareholders of the common shares and to receive dividends if, as, and when declared by the Board of Directors of our company. Holders of common shares are also entitled to participate, pro rata to their holding of common shares, in any distribution of the assets of our company upon its liquidation, dissolution or winding-up. The series A preferred shares, as set forth in our Articles of Incorporation, entitle our company to redeem all or any part of these shares subject to certain terms and conditions as set forth therein. These series A preferred shares are entitled to a dividend at a rate of $1.375 per annum per share.

Our company has not issued any restricted securities.

CREDIT RATINGS

Our company's corporate credit ratings from approved rating organizations are as follows:

Rating Agency	Short-term Debt	Long-term Debt
Standard & Poor's Rating Services Inc. ("S&P")	A-1	A+
DBRS Limited ("DBRS")	R-1 (middle)	A (high)
Moody's Investors Services Inc. ("Moody's")	Prime-1	Aa3

The following information relating to credit ratings is based on information made available to the public by the rating agencies.

Credit ratings are intended to provide investors with an independent measure of the credit quality of an issue of securities. The rating agencies rate long-term debt instruments by rating categories ranging from a high of "AAA" to a low of "D" ("C" in the case of Moody's). Long-term debt instruments which are rated in the A category by S&P mean the obligor has a strong capacity to meet its financial commitments but are considered somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher rated categories. However, the obligor's capacity to meet its financial commitments and obligations is still strong. S&P utilizes a "+" or a "-" modifier to indicate the relative standing within the rating category. Long-term debt instruments which are rated in the A category by DBRS are considered to be of a satisfactory credit quality, with substantial protection of interest and principal. Entities in the "A" category, however, are considered to be more susceptible to adverse economic conditions and have greater cyclical tendencies than higher-rated securities. The "high" modifier indicates relative standing within this rating category by DBRS. Long-term debt instruments which are rated in the Aa category by Moody's are judged to be of high quality and are subject to very low credit risk. Moody's applies numerical modifiers to each generic rating classification from Aa to Caa. The modifier 3 indicates a ranking in the lower end of that generic rating category.

The ratings mentioned above are not a recommendation to purchase, sell or hold our company's debt securities and do not comment as to market price or suitability for a particular investor. There can be no assurance that the ratings will remain in effect for any given period of time or that the ratings will not be revised or withdrawn entirely by any or all of S&P, DBRS and Moody's at any time in the future if in their judgment circumstances so warrant.

MARKET FOR SECURITIES

Our Debentures (7.15%) due 2010, Debentures (7.35%) due 2030, Series 1 Notes (6.40%) due 2011, Series 2 Notes (6.93%) due 2032, Series 3 Notes (5.77%) due 2012, Series 4 Notes (6.35%) due 2034, Series 5 Notes (6.59%) due 2043, Series 9 Notes (5.36%) due 2036, Series 10 Notes (4.640%) due 2016, Series 11 Notes (5.000%) due 2046, Series 12 Notes (4.89%) due 2037, Series 13 Notes (5.18%) due 2017, Series 14 Notes (4.08%) due 2011, Series 15 Notes

(5.00%) due 2013, Series 16 Notes (3.89%) due 2010 and Series 17 Notes (6.03%) due 2039 are currently outstanding and are not listed on any exchange or similar market for securities.

Trading Price and Volume

The debt securities issued by our company are not listed on a recognized exchange or quoted on a recognized quotation and trade reporting system.

Prior Sales

Our company issued the following tranches of medium term notes in 2008:

Note	Par Value (M) ($)	Sale Price ($)	Gross Proceeds ($)
Series 13 (5.18%) due 2017	300	102.547	$307,641,000
Series 14 (4.08%) due 2011	250	99.983	$249,957,500
Series 15 (5.00%) due 2013	400	99.890	$399,560,000
Series 16 (3.89%) due 2010	100	99.990	$99,990,000

DIRECTORS AND OFFICERS

Directors

The following table sets forth the name, municipality of residence and principal occupation of each of our directors, as of December 31, 2008.

Name and Municipality of Residence	Principal Occupation
Douglas E. Speers [2][3][5][6][7] Coldwater, Ontario Canada (Director since November 10, 2005 and Chair since December 8, 2008)	Chair of the Board of Directors of Hydro One Inc. Chairman and Director, Emco Corporation
Sami Bébawi [2][4][5] Outremont, Québec Canada (Director since October 8, 2004)	Advisor to the President, SNC-Lavalin Group Inc. President, Geracon Inc.
Kathryn A. Bouey [3][5][6] Toronto, Ontario Canada (Director since March 30, 2007)	President, TBG Strategic Services Inc. Corporate Director

Name and Municipality of Residence	Principal Occupation
Murray J. Elston [1] [4] Manotick, Ontario Canada (Director since June 11, 2002)	President and CEO, Canadian Nuclear Association
Laura Formusa Toronto, OntarioCanada (Director since March 30, 2007)	President and Chief Executive Officer, Hydro One Inc.
Don MacKinnon [4] [5] Chatsworth, Ontario Canada (Director since June 11, 2002)	President, Power Workers' Union
Michael J. Mueller [1] [2] [6] Tecumseh, Ontario Canada (Director since March 30, 2007)	Corporate Director
Walter Murray [1] [3] [6] Bracebridge, Ontario Canada (Director since November 10, 2005)	Corporate Director
Robert L. Pace [1] [3] Halifax, Nova Scotia Canada (Director since March 30, 2007)	President and Chief Executive Officer, The Pace Group Ltd.
Gale Rubenstein [2] [4] Toronto, Ontario Canada (Director since March 30, 2007)	Partner, Goodmans LLP

(1) Member of the Audit and Finance Committee

(2) Member of the Corporate Governance Committee

(3) Member of the Human Resources and Public Policy Committee

(4) Member of the Regulatory and Environment Committee

(5) Member of the Health and Safety Committee

(6) Member of the Business Transformation Committee

(7) Douglas E. Speers was appointed Chair of the Board of Directors of Hydro One Inc., on an interim basis, on December 8, 2008, replacing James Arnett who was Chair of the Board from March 31, 2008 until his resignation on December 8, 2008 following his appointment as Special Advisor to the Government of Canada and the Province on the auto sector's restructuring plans. Having resigned as a Special Advisor to the Government of Canada, Mr. Arnett was re-appointed as Chair of the Board of Directors effective February 17, 2009.

Douglas E. Speers is Chairman and Director of Emco Corporation, a leading Canadian distributor of building materials for the residential, commercial and industrial construction markets. Prior to his appointment as Chairman of Emco Corporation, Mr. Speers was Emco's President and CEO from 1997 - 2004. Between 1971 and 1988, he held several senior positions with Imperial Oil Ltd. in Canada and Exxon International in New York City. Mr. Speers is a Professional Engineer - Province of Ontario, a member of the Advisory Board of the Richard Ivey School of Business, and Chair and Director of the Ivey Management Services Company. He is a member of the boards of a number of privately-held companies and has been a Director of our company since November 10, 2005.

Sami Bébawi is the president of his own construction project management company, Geracon Inc. From 1999 until December 31, 2006 he was an Executive Vice President of SNC-Lavalin Group Inc. and member of the Office of the President and President of the heavy construction company Socodec Inc. Mr. Bébawi also had the corporate responsibility in project management policy at SNC-Lavalin Group Inc. He is currently Advisor to the President of SNC-Lavalin Group Inc. He is an engineering graduate with a Masters Degree and has several years of experience in designing and building thermal, hydro and nuclear power plants. Mr. Bébawi is a Member of the Ordre des ingénieurs du Québec and is a conjunct professor at Concordia University, Montreal. He is also Vice Chair and Director of Aecedge Inc. and Director of SNC-Lavalin Gulf Contractors L.L.C. Mr. Bébawi has been a Director of our company since October 8, 2004.

Kathryn A. Bouey is President of TBG Strategic Services Inc. (formerly Kathryn Bouey & Associates Ltd.), a management consulting firm. From 2001 to 2005, Ms. Bouey was the Deputy Minister of the Management Board Secretariat, Province of Ontario and previously held other senior management positions with the Province, including: Deputy Minister of Intergovernmental Affairs (1999-2001); and Assistant Deputy Minister, Corporate Services Group, Ministry of Health and Long-Term Care (1997-1999). She is currently a Governor of Sheridan College and a Director of St. Joseph's Health Centre. Previously, she held the position of Chair of the Ontario Civil Service Commission and has served on the boards of the Canadian Comprehensive Auditing Foundation, Ontario Power Generation, the Ontario Financing Authority and the Ontario Pension Board. Ms. Bouey obtained a Master of Arts (Economics) from Carleton University in 1981 and was certified by the Institute of Corporate Directors in 2006. She has been a Director of our company since March 30, 2007.

Murray J. Elston has been the President and CEO of the Canadian Nuclear Association ("CNA"), since January 5, 2004. The CNA is a non-profit organization that represents the nuclear industry

in Canada and promotes the development and growth of nuclear technologies for peaceful purposes. He previously served as President of Canada's Research-Based Pharmaceutical Companies, a national association representing over 60 research-based pharmaceutical companies, to which he was appointed in November 1998. From 1981 to 1994, he served as a Liberal MPP in the Ontario Legislature, where he held the positions of Minister of Health, Chairman of Management Board, Minister of Financial Institutions and Chairman of the Public Accounts Committee. Mr. Elston is Chair of the Walkerton Clean Water Centre and the Canadian Nurses Foundation. He is also Past Chair of the Board of Directors of the University of Ottawa Institute of Mental Health and Research and Energy Dialogue Group. He serves on the Board of the Canadian Centre for Energy Information. Mr. Elston has been a Director of our company since June 11, 2002.

Laura Formusa was appointed President and Chief Executive Officer, Hydro One Inc., on November 23, 2007, having served as the company's acting President and Chief Executive Officer since December 8, 2006. Ms. Formusa was appointed Hydro One's General Counsel and Secretary in 2003. She held various senior positions until being appointed General Counsel of Hydro One Networks Inc. in 2000. Ms. Formusa earned her Bachelor of Laws degree at Osgoode Hall Law School and was admitted to the Law Society of Upper Canada in 1980, following her call to the Bar of Ontario. She has been a Director of our company since March 30, 2007.

Don MacKinnon has been President of the Power Workers' Union, an electricity industry workers union, since May 2000 and a lineman by trade since 1971. He was Vice-President of the Union for 11 years prior to being elected President. In 2000, Mr. MacKinnon was appointed by the Minister of Energy, Science and Technology to the Electricity Transition Committee. He was a member of the Board of Directors of the Electrical and Utilities Safety Association and the Retail Management Board of Ontario Hydro. In 2003, Mr. MacKinnon was appointed by the Minister of Energy to the government's Electricity Conservation and Supply Task Force. In 2005, Mr. MacKinnon became a member of the Canadian Nuclear Association's Board of Directors. He is also a member of the National Round Table on the Environment and the Economy. Mr. MacKinnon has been a Director of our company since June 11, 2002.

Michael J. Mueller is a former Global leader of PricewaterhouseCoopers' (PwC) Private Company Services/Middle Market Practice and a former member of PwC's Global Audit Leadership Team, Global Advisory Leadership Team and the Global Markets Council. Prior to his retirement from PwC in July 2007, his previous positions with the firm also included National Managing Partner for Canada and Senior Relationship Partner for a number of the firm's most significant clients. He is also a Chartered Accountant, a Certified Insolvency Practitioner, and a Chartered Business Valuator. In December 2008, Mr. Mueller was appointed to the Ontario Economic Advisory Panel by the Minister of Finance of Ontario. Mr. Mueller's past community involvement includes: member of the Board of Governors of the Stratford Shakespearean Festival of Canada; President of the Windsor Symphony Society; and President, Better Business Bureau of Windsor and Essex Counties. He has been a Director of our company since March 30, 2007.

Walter Murray is a former Vice-Chairman and member of the Executive Committee of RBC Capital Markets, an international corporate and investment bank. Prior to his retirement from the RBC Royal Bank in April 2005, his 38-year career included Senior Executive Investment

Banking responsibility for overseeing and directing all financial and advisory activity with a portfolio of major Canadian and International accounts; Executive head of Corporate Banking activities across Canada, and several other Executive postings, including serving as Regional Executive for RBC's Midwestern USA Corporate Banking operations. Since 2000, Mr. Murray has been a member of Ivernia Inc.'s Board of Directors and Chair of its audit committee. Mr. Murray has been a Director of our company since November 10, 2005.

Robert L. Pace is the President and Chief Executive Officer of The Pace Group Ltd. The Pace Group owns and operates a number of companies across Atlantic Canada, including: Maritime Broadcasting System Ltd., a 24 radio station group; MBS Realty Ltd.; Green Waste Systems Inc. and Shredder's. He began his professional career with the Halifax law firm Chandler Moore, where he practiced family and commercial law. Between 1981 and 1984, Mr. Pace served as Atlantic Advisor to the Prime Minister of Canada. Mr. Pace is currently a member of the Board of Directors of Canadian National Railway Company; Overland Realty Limited (Chairman of the Board); Canadian Health Care Consulting Services Ltd.; High Liner Foods Incorporated; the Atlantic Salmon Federation; the Asia Pacific Foundation; and the Public Gardens Restoration Committee (Halifax). Mr. Pace was called to the Nova Scotia Bar in 1981 following the completion of his Bachelor of Laws degree at Dalhousie University, where he also completed an MBA in 1977. He has been a Director of our company since March 30, 2007.

Gale Rubenstein is a partner of the law firm Goodmans LLP and a member of the firm's Executive Committee. She practices law primarily in the areas of commercial insolvency and restructuring with emphasis on financial institutions, both domestic and international, and on pension restructurings. Ms. Rubenstein was senior counsel to the liquidators of numerous financial institutions and has been counsel to the Superintendent of Financial Institutions (Canada) and the Superintendent of Financial Services (Ontario). She has authored numerous papers on the insolvency of insurance companies and banks, and is update author of LexisNexis Canada's Insurance Companies Act: Legislation and Commentary. She obtained her Bachelor of Law degree from Osgoode Hall Law School and is a current member of the Insolvency Institute of Canada; Insol International; and a Director of the Canadian Lawyer Liability Assurance Society. She has been a Director of our company since March 30, 2007.
Each director is elected annually to serve for one year or until his or her successor is elected or appointed.

Officers

The following table sets forth the name, municipality of residence and position of each of our executive officers as of December 31, 2008. On February 3, 2009, Hydro One announced the appointment of Sandy Struthers as its new Chief Financial Officer effective February 12, 2009. Beth Summers resigned as Chief Financial Officer effective the same date. On March 1, 2009 Geoff Ogram assumed the newly-created role of Special Advisor to the President, and, in addition to his former role as Vice-President Corporate Projects, Carmine Marcello assumed the role of Vice President, Asset Management.

Name and Municipality of Residence	Position With Our Company
Laura Formusa Toronto, Ontario	President and Chief Executive Officer

Name and Municipality of Residence	Position With Our Company
Canada	
Beth Summers Oakville, Ontario Canada	Executive Vice President and Chief Financial Officer (until February 12, 2009)
Sandy Struthers Toronto, Ontario Canada	Chief Financial Officer (effective February 12, 2009)
Joseph Agostino Toronto, Ontario Canada	General Counsel
Myles D'Arcey Toronto, Ontario Canada	Senior Vice President, Customer Operations
Tom Goldie Mississauga, Ontario Canada	Senior Vice President, Corporate Services
Nairn McQueen Dundas, Ontario Canada	Vice President, Engineering & Construction Services
Geoff Ogram Toronto, Ontario Canada	Vice President, Asset Management (until March 1, 2009, when he assumed the newly created role of Special Advisor to the President)
Carmine Marcello Thornhill, Ontario Canada	Vice President, Asset Management and Corporate Projects (effective March 1, 2009)
Wayne Smith Toronto, Ontario Canada	Vice President, Grid Operations

Laura Formusa's biographical information is presented above under "Directors".

Beth Summers was appointed as Chief Financial Officer on May 7, 2004 after serving as Corporate Controller of Hydro One Networks Inc. Prior to joining our company in 2001, Ms.

Summers served as Senior Manager, Assurance & Advisory Services with Ernst & Young LLP. Ms. Summers resigned from our company effective February 12, 2009.

Joseph Agostino was appointed as General Counsel on December 13, 2007, after having served as Acting General Counsel since December 8, 2006. He joined Ontario Hydro in 1995 and has previously held the position of Assistant General Counsel of Hydro One Networks Inc.

Sandy Struthers was appointed as Chief Financial Officer effective February 12, 2009. Mr. Struthers joined Hydro One in 2000 as a Director in the Finance area and has held a number of senior positions in Finance, including Director, Financial Strategy and Director, Merger & Acquisitions Finance. In 2005, he was appointed to the position of Chief Information Officer where he implemented a number of significant advancements in our company's IT infrastructure.

Myles D'Arcey was appointed as Senior Vice President, Customer Operations of Hydro One Networks Inc. on May 1, 2005. Mr. D'Arcey is also President and Chief Executive Officer of Hydro One Remote Communities Inc. He joined Ontario Hydro in 1978 and has held the position of Vice President, Station Services of Hydro One Networks Inc.

Tom Goldie was appointed as Senior Vice-President, Corporate Services of Hydro One Networks Inc. on September 16, 2002. He joined Ontario Hydro in 1977 and has held the position of Vice-President, Human Resources of Hydro One Inc.

Nairn McQueen was appointed as Vice President, Engineering & Construction Services of Hydro One Networks Inc. on August 28, 2002. Prior to joining Hydro One Network Services Inc. in 2000 as Director of Engineering, Mr. McQueen was V.P., Engineering and Project Management Services for Agra Monenco.

Geoff Ogram was appointed Special Advisor to the President effective March 1, 2009 after serving as Vice President, Asset Management of Hydro One Networks Inc. from January 1, 2005. He joined Ontario Hydro in 1981 and has held the position of Vice President, Strategy & Development of Hydro One Networks Inc.

Carmine Marcello was appointed as Vice-President, Asset Management and Corporate Projects of Hydro One Networks Inc. on March 6, 2009 after serving as Vice-President, Corporate Projects of Hydro One Networks Inc. from March 21, 2007. Carmine joined Ontario Hydro in 1987 and has held a number of senior positions including Director, System Investment and Director, Ontario Grid Control Centre Transformation.

Wayne Smith was appointed Vice President, Grid Operations of Hydro One Networks Inc. on January 1, 2005. He joined Ontario Hydro in 1980 and has held the position of Director of Investment Planning and Asset Management of Hydro One Networks Inc.

There is no family relationship between any director or officer and any other director or officer.

Indebtedness of Directors and Executive Officers

As of March 1, 2009 and since the beginning of the most recently completed financial year of Hydro One, no director, executive officer, employee, former director, former executive officer or former employee or associate of any director or executive officer of Hydro One or any of its

subsidiaries had any outstanding indebtedness to Hydro One or any of its subsidiaries except routine indebtedness or had any indebtedness that was the subject of a guarantee, support agreement, letter of credit or other similar arrangement or understanding provided by Hydro One or any of its subsidiaries.

INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS

Relationships with the Province and Other Parties

Overview

The Province of Ontario owns all of our outstanding shares. As a result, the Province has the power to control all governance decisions affecting us, including the composition of our Board of Directors. Accordingly, the Province exercises control over our policies, the acquisition or disposition of assets, the incurrence of further debt and the payment of dividends to holders of our common and preferred shares.

The OEB is the principal regulator of Ontario's electricity industry. The Province appoints the members of the OEB and fills any vacancies on the OEB. The OEB is obligated to implement approved directives of the Province concerning general policy and objectives to be pursued by the OEB and other directives aimed at addressing existing or potential abuses of market power by industry participants. The IESO directs the operation of our transmission system. The board of directors of the IESO, other than its chief executive officer, is appointed by the Province in accordance with the regulations in effect from time to time under the *Electricity Act, 1998*.

The OPA is mandated to forecast supply and demand of electricity over the medium and long term and to conduct planning and implement measures to meet the supply and demand needs. Its board of directors is appointed by the Province.

Transfer Orders

The transfer orders pursuant to which we acquired Ontario Hydro's electricity transmission, distribution and energy services businesses as of April 1, 1999 did not transfer any asset, right, liability or obligation where the transfer would constitute a breach of the terms of any such asset, right, liability or obligation or a breach of any law or order. The transfer orders also did not transfer title to some assets located on lands held for bands or bodies of Indians under the *Indian Act* (Canada). The transfer of title to these assets did not occur because authorizations originally granted by the Canadian Minister of Indian and Northern Affairs for the construction and operation of these assets could not be transferred without the consent of such Minister and the relevant Indian bands or bodies or, in several cases, because the authorizations had either expired or had never been properly issued. These assets consist primarily of approximately 82 km of transmission lines and distribution lines used to deliver electricity on reserves (of which 14 km of lines are used solely for serving customers off the reserves). OEFC holds these assets.

We are obligated under the transfer orders to manage both the assets held in trust until we have obtained all consents necessary to complete the transfer of title to these assets to us and the assets otherwise retained by OEFC that relate to our businesses. We have entered into an agreement with OEFC under which we are obligated, in managing the assets, to take instructions from OEFC if our actions could have a material adverse effect on it. OEFC has retained the right to

take control of and manage the assets, although it must notify and consult with us before doing so and must exercise its powers relating to the assets in a manner that will facilitate the operation of our businesses. The consent of OEFC is also required prior to any disposition of these assets.

The Province also transferred officers, employees, assets, liabilities, rights and obligations of Ontario Hydro in a similar manner to its other successor corporations. These transfer orders include a dispute resolution mechanism to resolve any disagreement among the various transferees with respect to the transfer of specific assets, liabilities, rights or obligations.

The transfer orders do not contain any representations or warranties from the Province or OEFC with respect to the transferred officers, employees, assets, liabilities, rights and obligations. Furthermore, under the *Electricity Act, 1998*, OEFC was released from liability in respect of all assets and liabilities transferred by the transfer orders, except for liability under our indemnity from OEFC as discussed below. By the terms of the transfer orders, each transferee indemnifies OEFC with respect to any assets and liabilities not effectively transferred and is obligated to take all reasonable measures to complete the transfers where the transfers were not effective.

Indemnities

OEFC indemnified us with respect to the failure of the transfer orders to transfer any asset, right or thing or any interest therein related to our business to us and some of our subsidiaries, some adverse claims or interests of third parties or based on title deficiencies arising from the transfer orders, except for some claims and rights of the Crown, and claims related to any equity account previously referred to in the financial statements of Ontario Hydro including amounts relating to any judgment, settlement or payment in connection with litigation initiated by some utilities commissions. The Province has unconditionally and irrevocably guaranteed to us and our subsidiaries the payment of all amounts owing by OEFC under its indemnity.

The indemnity specifically excludes any matter for which we have agreed or are required to indemnify OEFC pursuant to or in connection with any transfer order. It also excludes any claim related to any aboriginal title or rights or the absence of a permit, right-of-way, easement or similar right in respect of lands held for Indian bands under the *Indian Act* (Canada). It also excludes any payment made, or loss, expense or liability incurred by us as a result of the failure of a transfer order to transfer any asset of Ontario Hydro described in the provisions of the transfer order relating to ineffective transfers.

The indemnity does not cover the first $10,000 in value of each claim and only applies to the amount by which the total of all claims exceeds $10 million. We are obliged to pay OEFC a fee for the indemnity of $5 million per year until such time as the parties agree that the indemnity should be terminated. We anticipate that we will require the indemnity until all indemnifiable claims have been identified and finally determined by a non-appealable court order. The indemnity ceases to be available to any of our subsidiary corporations if we cease to control them unless the cessation of ownership results from the sale of the shares of a subsidiary in connection with the enforcement of security on such shares by an arm's-length creditor of Hydro One. The indemnity can be assigned under some conditions with the consent of the Minister of Finance.

The Province has also agreed to indemnify the directors of Hydro One for any liabilities reasonably incurred by them in respect of any civil, criminal or administrative action or proceeding to which they are made a party to the extent that these liabilities result from a claim

or determination that their approval of the indemnity by OEFC constituted a breach of their duty to exercise the care, diligence or skill that a reasonably prudent person would exercise in comparable circumstances.

We have indemnified OEFC in respect of the damages, losses, obligations, liabilities, claims, encumbrances, penalties, interest, deficiencies, costs and expenses arising from matters relating to our business and any failure by us to comply with our obligations to OEFC under agreements dated as of April 1, 1999. These obligations include obligations to employ the employees transferred to us under the transfer orders, make and remit employee source deductions, i.e., tax withholding amounts, and employer contributions, manage the real and personal properties which OEFC continues to hold in trust or otherwise and take any necessary action to transfer all of these properties to us, to pay realty taxes and other costs, provide access to books and records and to assume other responsibilities in respect of the assets held by OEFC in trust for us.

Transmission Corridors

On June 27, 2002, the Province passed the *Reliable Energy and Consumer Protection Act, 2002* that provided for, among other things, ownership of all transmission corridor and abutting lands to be transferred from us to the Province in exchange for a statutory right to use the lands for transmission and distribution purposes effective December 31, 2002. Corridor land totalling 49,673 acres with a net book value of approximately $259 million was transferred to the Province. In addition, ownership of land assets with a net value of approximately $7 million, not then in use, was transferred to the Province and applied as a reduction of shareholder's equity. We also retained the obligation to incur certain ongoing expenditures related to our use of this land, including maintenance, property taxes and any future environmental remediation work that may be required by the Province. The OEB is authorized to restrict or discontinue any use of the transmission corridor lands that interferes with the transmission system. The Province later decided to return certain lands to us. During 2003-2005, the Province returned approximately 7,271 acres of lands with a net book value of $38.2 million.

Operational Matters

Hydro One receives its revenues, which are in part collected by the IESO from customers, in accordance with the rules established under the *Electricity Act, 1998* and the *Ontario Energy Board Act, 1998*, as amended from time to time.

Hydro One and the IESO have entered into an operating agreement, which took effect in May 2002, setting out the specific responsibilities of both parties relating to the provision of transmission service. Hydro One also purchases power from the IESO administered spot market.

Hydro One has several service agreements with the other successor corporations to Ontario Hydro, primarily OPG. These services include field and engineering, logistics, corporate, telecommunications and information technology services.

Payments in Lieu of Corporate Taxes

We and our subsidiaries are exempt from taxes under the *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario) because we are wholly owned by the Province and each of our subsidiaries is, in turn, wholly owned (directly or indirectly) by us. However, pursuant to the

Electricity Act, 1998, we and each of our subsidiaries are required to pay amounts to the OEFC, which are referred to as payments in lieu of corporate taxes or proxy taxes, in respect of each taxation year, generally equal to the amount of tax that we would be liable to pay under the *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario) if we were not exempt from taxes thereunder.

Memorandum of Agreement

We entered into a memorandum of agreement with the Province in March 2008 relating to our mandate, responsibilities, performance expectations and executive compensation. Under this agreement, we must prepare investment plans for new transmission and distribution projects and prioritize investments in transmission and distribution capacity to support projects necessary to maintain ongoing grid security and reliability. This agreement also requires that we undertake special initiatives communicated from time to time by the Province by way of unanimous shareholder agreement or declaration in accordance with the provisions of the *Business Corporations Act* (Ontario). Additionally, this agreement requires that we obtain approval from the Province in advance of any proposal to issue or transfer shares in Hydro One or its subsidiaries, any major transaction, including the sale of assets, which would potentially have a material effect on the financial interest of the Province or our ability to make payments to OEFC or payments in lieu of corporate taxes (proxy taxes) under the *Electricity Act, 1998*.

Effective September 24, 2008, the Province made a declaration pursuant to the memorandum of agreement and Section 108 of the *Business Corporations Act* (Ontario) (the "Shareholder Directive") pertaining to off-shoring of jobs under the outsourcing arrangement with Inergi LP (the "Inergi Agreement"). The declaration allows the Province to assume all decision-making power in respect of the off-shoring of jobs under the Inergi Agreement and removes these powers from the Board of Directors of Hydro One. The directors and officers of Hydro One are charged with performing that which is necessary to carry out the intention of the Shareholder Directive. Copies of the memorandum of agreement and the Shareholder Directive have been filed with the securities regulatory authorities in each province of Canada and are available at www.sedar.com.

TRUSTEES AND REGISTRARS

The trustee and registrar for our company's debt securities is Computershare Trust Company of Canada, located in Toronto, Ontario.

The U.S. trustee and registrar for our company's debt securities is Bank of Nova Scotia Trust Company of New York located in New York, New York.

MATERIAL CONTRACTS

Except for the following, since January 1, 2002, our company did not enter into any material contracts, other than contracts in the ordinary course of business:

(a) (i) a third supplemental trust indenture dated as of January 31, 2003 relating to the issuance of Series 4 Notes in the aggregate principal amount of $1,000,000,000, of which $200,000,000 was drawn down on January 31, 2003, $120,000,000 was drawn down on June 25, 2004 and $65,000,000

was drawn down on August 24, 2004, pursuant to the Trust Indenture dated as of June 4, 2001 between Hydro One and Computershare Trust Company of Canada (the "Trust Indenture");

(ii) a fourth supplemental trust indenture dated as of April 22, 2003 relating to the issuance of Series 5 Notes in the aggregate principal amount of $1,000,000,000, of which $250,000,000 was drawn down on April 22, 2003 and $65,000,000 was drawn down on August 20, 2004, pursuant to the Trust Indenture;

(iii) a fifth supplemental trust indenture dated as of June 23, 2003 relating to the issuance of Series 6 Notes in the aggregate principal amount of $1,000,000,000, of which $500,000,000 was drawn down on June 23, 2003, pursuant to the Trust Indenture;

(iv) a sixth supplemental trust indenture dated as of February 24, 2004 relating to the issuance of Series 7 Notes in the aggregate principal amount of $1,000,000,000, of which $250,000,000 was drawn down on February 24, 2004, and $150,000,000 was drawn down on May 19, 2005, pursuant to the Trust Indenture;

(v) a seventh supplemental indenture dated as of November 15, 2004 relating to the issuance of Series 8 Notes in the aggregate principal amount of $1,000,000,000, of which $400,000,000 was drawn down on November 15, 2004, pursuant to the Trust Indenture;

(vi) an eighth supplemental indenture dated as of May 19, 2005 relating to the issuance of Series 9 Notes in the aggregate principal amount of $1,000,000,000, of which $350,000,000 was drawn down on May 19, 2005 and $250,000,000 was drawn down on April 24, 2006, pursuant to the Trust Indenture;

(vii) a ninth supplemental trust indenture dated as of March 3, 2006 relating to the issuance of Series 10 Notes in the aggregate principal amount of $1,000,000,000, of which $300,000,000 was drawn down on March 3, 2006 and $150,000,000 was drawn down on August 22, 2006, pursuant to the Trust Indenture;

(viii) a tenth supplemental trust indenture dated as of October 19, 2006 relating to the issuance of Series 11 Notes in the aggregate principal amount of $1,000,000,000, of which $75,000,000 was drawn down on October 19, 2006, pursuant to the Trust Indenture;

(ix) an eleventh supplemental trust indenture dated as of March 13, 2007 relating to the issuance of Series 12 Notes in the aggregate principal amount of $1,000,000,000, of which $400,000,000 was drawn on March 13, 2007, pursuant to the Trust Indenture;

(x) a twelfth supplemental trust indenture dated as of October 18, 2007 relating to the issuance of Series 13 Notes in the aggregate principal amount of $1,000,000,000, of which $300,000,000 was drawn down on October 18, 2007 and $300,000,000 was drawn down on March 3, 2008, pursuant to the Trust Indenture;

(xi) a thirteenth supplemental trust indenture dated as of March 3, 2008 relating to the issuance of Series 14 Notes in the aggregate principal amount of $1,000,000,000, of which $250,000,000 was drawn down on March 3, 2008, pursuant to the Trust Indenture;

(xii) a fourteenth supplemental trust indenture dated as of November 10, 2008 relating to the issuance of Series 15 Notes in the aggregate principal amount of $1,000,000,000, of which $400,000,000 was drawn down on November 10, 2008 and $200,000,000 was drawn down on January 14, 2009, pursuant to the Trust Indenture;

(xiii) a fifteenth supplemental trust indenture dated as of November 19, 2008 relating to the issuance of Series 16 Notes in the aggregate principal amount of $1,000,000,000, of which $100,000,000 was drawn down on November 19, 2008 and $100,000,000 was drawn down on January 13, 2009, pursuant to the Trust Indenture; and

(xiv) a sixteenth supplemental trust indenture dated as of March 3, 2009 relating to the issuance of Series 17 Notes in the aggregate principal amount of $1,000,000,000, of which $300,000,000 was drawn down on March 3, 2009, pursuant to the Trust Indenture.

Each of these supplemental trust indentures supplement the terms of the Trust Indenture which contains customary covenants and representations by our company for the public issuance of debt securities in the Canadian market.

(b) a Dealer Agreement dated June 21, 2007 between our company and BMO Nesbitt Burns Inc., Casgrain & Company Limited, CIBC World Markets Inc., HSBC Securities (Canada) Inc., Laurentian Bank Securities Inc., National Bank Financial Inc., RBC Dominion Securities Inc., Scotia Capital Inc. and TD Securities Inc. (collectively, the "Dealers") relating to the public offering of unsecured medium term notes of Hydro One in a maximum aggregate principal amount of up to $2,500,000,000. The Dealer Agreement provides for the appointment of the Dealers as non-exclusive agents of Hydro One to solicit, from time to time, offers to purchase its medium term notes in Canada and, in certain circumstances, the United States.

Copies of these documents are available on www.sedar.com.

INTERESTS OF EXPERTS

For the year ended December 31, 2008, KPMG LLP provided the following services to our company:

(a) quarterly review of our company's consolidated financial statements;

(b) annual audit of our company's consolidated financial statements;

(c) annual audit of Hydro One Networks Inc.'s transmission and distribution businesses, Hydro One Remote Communities Inc.'s and Hydro One Brampton Networks Inc.'s financial statements; and

(d) annual audit of our company's pension fund and the following companies which hold our alternative asset investments: HOPF-HFG Investments Ltd., HOPF – HFM Investments Ltd., HOPF-PEJ Investments Ltd. and HOPF-PEP Investments Ltd.

For the year ended December 31, 2007, Ernst & Young LLP provided the following services to our company:

(a) quarterly review of our company's consolidated financial statement;

(b) annual audit of our company's consolidated financial statements

(c) annual audit of Hydro One Networks Inc.'s transmission and distribution business, Hydro One Remote Communities Inc.'s and Hydro One Brampton Network Inc.'s financial statements; and

(d) annual audit of our company's pension fund and the following companies which hold our alternative asset investments: HOPF_HFG Investment Ltd., HOPF_HFM Investments Ltd., HOPF_PEJ Investments Ltd. and HOPF-PEP Investments Ltd.

Each of KPMG LLP and Ernst & Young LLP is independent in Canada in accordance with its rules of professional conduct.

KPMG LLP has provided services in respect of the documentation, evaluation and enhancement of internal controls over financial reporting and disclosure controls consistent with the requirements of applicable securities law. This work was completed in early 2007.

Mercer Human Resource Consulting LLC provides the following services to our company:

(a) annual accounting actuarial valuation (valuation report prepared);

(b) tri-annual funding actuarial valuation (last valuation completed as of December 31, 2006, filed in September 2007); and

(c) annual accounting actuarial valuation for supplementary pension plan for purposes of letters of credit (valuation report prepared).

ADDITIONAL INFORMATION

Additional Information about Hydro One is available on SEDAR (System for Electronic Document Analysis and Retrieval) at www.sedar.com

As our sole shareholder is the Province, we are not required to prepare an information circular. Additional financial information is contained in our audited comparative consolidated financial statements, together with the auditors' report thereon, and our Management's Discussion and Analysis for our most recently completed fiscal year, each of which may be found on SEDAR at www.sedar.com

STATEMENT OF EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

Executive Compensation Program

The objective of Hydro One's executive compensation program is to establish pay levels based on performance, to be competitive with Canadian utility and energy companies, both publicly and privately owned, and to attract, motivate and retain executives. The recruitment and retention of a management team with the skills necessary to sustain and develop a safe, efficient and reliable electricity delivery system is critical for Hydro One's current and long-term success. Considering the risks associated with our employee demographics and the competitive market for skilled energy sector employees described below, attracting and retaining knowledgeable and motivated executives is a fundamental premise of our executive compensation program and strategy.

Hydro One faces the same challenges that other Canadian utilities presently face, and in particular the same challenges confronting the electricity industry in North America, with respect to employee demographics and the competitiveness of the market for skilled employees. The Electricity Sector Council recently released its national Labour Market Information Study, which confirms significant staff shortages in the executive and management ranks of the sector across Canada over the next five years. By the end of 2008, more than 20% of Hydro One's employees were eligible for retirement and by 2010 there may be more than 40% eligible to retire. Typically, employees working in head office functions retire shortly after they become eligible to retire while those working in the field environment generally work until reaching 35 years of service or maximizing their pension benefit. To be successful, Hydro One needs to attract and retain sufficient qualified staff to replace those retiring as well as to position the company for its large work and infrastructure program. This will be challenging as the labour market for the industry continues to be highly competitive. Thus, compensation that will attract the qualified people is a key objective of our program.

Many Hydro One employees possess experience and skills that are highly sought after by other organizations both inside and outside the electricity sector. Hydro One has lost management staff in executive positions and potential successors for executive positions to opportunities in other electricity sector positions across Canada and to positions outside the electricity sector. Accordingly, retention of executives is an important objective of our executive compensation strategy.

Our compensation program is designed to reward ongoing performance through the base salary component of the program, and longer term and/or project based performance through the short term incentive plan (the "Incentive Plan"). Overall, the program is intended to reward behaviour which will drive corporate performance and productivity and which will drive the implementation of corporate strategy. The company's overall compensation objectives are to ensure that base salary and Incentive Plan values are within the 50th percentile of the target market.

Elements of Compensation

Compensation for executive officers consists of a base salary, performance-based pay through the Incentive Plan, pension and health and dental benefits, each of which is described in more detail below. Each of Ms. Formusa, Ms. Summers, Mr. Goldie, Mr. McQueen and Mr. D'Arcey was entitled under their respective employment agreements to these elements of compensation. Hydro One does not provide its senior management with perquisites such as personal club memberships, car allowances, entertainment accounts or similar perquisites.

(1) Base Salary

Base (annual) salary is intended to compensate the Named Executive Officers ("NEOs") for day to day, ongoing performance. The Hydro One Board of Directors determines a range of base compensation for each NEO based on market comparisons and corporate performance.

The actual level of base salary, within the approved range for each executive officer, including the NEOs, is determined on the basis of job function and the individual's performance and experience. The President and Chief Executive Officer annually submits a base salary recommendation to the Human Resources and Public Policy Committee of the Board of Directors (the "HRPP Committee") for each of her direct reports. The HRPP Committee sets the base salary of such executives and then reports its decision to the Board of Directors. The HRPP Committee brings a base salary recommendation for the President and Chief Executive Officer to the Board of Directors for approval.

The positioning of the NEO within the range is based on the level of performance relative to the requirements of the position. The Hydro One Board of Directors establishes a base salary increase fund based on market comparisons and corporate performance. Performance is assessed on day-to-day performance in the role, both in terms of results and behaviours, and is often related to the level of experience in the role. The base salary increase is allocated among the NEOs based strictly on performance. Hydro One does not provide across-the-board or economic increases to its NEOs. An NEO's base salary may increase annually, but may not decrease.

Base salary is determined differently for NEOs depending on whether they became NEOs before or after the Agency Review Panel made recommendations in June of 2007. The result is three different methodologies for determining base salary: the pre-Agency Review Panel methodology, the post-Agency Review Panel methodology, and the current methodology, which is going to be followed in the future. Each will be described in turn.

<u>Pre-Agency Review Panel Methodology</u>

For individuals who were executive officers before the Agency Review Panel made its recommendations in June of 2007, the HRPP Committee established base salary ranges for the positions held by executive officers following a review of market data from peer group, industry and national surveys provided by independent consultants. The comparator group used by Hydro One for this purpose consists of Canadian utility and energy companies and similar industrial organizations, weighted 80/20 privately/publicly owned. Total compensation was established relative to the 75th percentile of total direct cash (i.e. salary policy plus target bonus) of this comparator group.

For this group, Hydro One uses a set of 44 comparators which represent primarily public and private sector energy related companies in Canada. The comparator list consists of 35 private sector companies and 9 public sector companies. Of the 44 companies, 18 are utilities or utility related companies. The companies vary in size. Of the 38 companies in the comparator group with publicly available financial information, approximately 47% were smaller than Hydro One based on revenues and assets, according to their most recent publicly available annual financial statements. Of the 17 utilities or utility-related companies in the comparator group with publicly available financial information, approximately 65% were smaller than Hydro One. Certain companies in the comparator group are not reportable segments of their reporting parent and therefore financial information was not available.

The list of companies in the comparator group is shown below:

Org Name	**Sector (Public / Private)**
ArcelorMittal Dofasco Inc.	Private
AstraZeneca Canada Inc.	Private
Barrick Gold Corporation	Private
Bayer Inc.	Private
Bell Canada	Private
British Columbia Hydro and Power Authority	Public
Bruce Power	Private
CN Rail	Private
Canadian Pacific Railway	Private
Dofasco Automotive Group	Private
Dofasco Tubular Products Corporation	Private
Domtar Inc.	Private
Dow Chemical Canada Inc.	Private
Emera Inc.	Private
Enbridge Gas Distribution Inc.	Private
Enbridge Inc.	Private
Enbridge International Inc.	Private
Enbridge Pipelines Inc.	Private
Enersource Hydro Mississauga	Public
Finning (Canada)	Private
Finning International Inc.	Private
Goodyear Canada Incorporated	Private
Government of Ontario	Public

Org Name	Sector (Public / Private)
Horizon Utilities Corporation	Public
Hydro-Québec	Public
Independent Electricity System Operator	Public
Ingersoll-Rand Canada Inc.	Private
John Deere Limited Canada	Private
NOVA Chemicals Corporation	Private
Nova Scotia Power Inc.	Private
Ontario Power Generation Inc.	Public
Petro-Canada	Private
Rio Tinto Alcan	Private
SaskPower	Public
Siemens Canada Limited	Private
Siemens Power Generation	Private
Syncrude Canada Ltd.	Private
Tembec Inc.	Private
Terasen Gas	Private
Toromont CAT	Private
Toronto Hydro Corporation	Public
Ultramar Ltée	Private
Vale Inco Limited	Private
Xstrata Nickel Canada	Private

Private	35
Public	9
Total	**44**

Post-Agency Review Panel Methodology

The Minister of Energy announced in June 2007 that all the recommendations of the Agency Review Panel were being accepted by the Province and requested us to support the initiative. Hydro One has complied with the relevant recommendations.

Based on the Agency Review Panel's recommendations, Hydro One implemented the following guidelines with respect to compensation of new executives and new senior management:

- Use comparative market data based on a 50/50 blend of public and private sector companies in determining total compensation.
- Establish total compensation relative to the 50th percentile of total direct cash (i.e. salary plus target bonus plus annualized net present value of long-term incentive, plus benefits plus pension) of the 50/50 blended market data.

As a result, for new executive officers, the HRPP Committee, entirely independent of management, developed a new comparator group with the assistance of the external compensation advisors, the Hay Group. The comparator group consists of 30 Canadian-based companies (15 public and 15 private), approximately 2/3 of which are utilities (primarily

electric). These companies vary in size with approximately 71% of the 28 companies in the comparator group with publicly available financial information being smaller in size when compared to Hydro One, based on both revenues and assets, according to their most recent publicly available annual financial statements. Two of the companies are not reportable segments of their reporting parent and therefore financial information was not available.

The list of comparator group companies is as follows:

Org Name	**Sector (Public / Private)**
Bell Canada	Private
British Columbia Hydro and Power Authority	Public
Bruce Power	Private
Business Development Bank of Canada	Public
Canada Mortgage and Housing Corporation	Public
Canada Post Corporation	Public
CN Rail	Private
Enbridge Gas Distribution Inc.	Private
Enersource Hydro Mississauga	Public
Farm Credit Canada	Public
Fortis Inc.	Private
Fortis Ontario Inc.	Private
Manitoba Telecom Services Inc.	Private
NB Power Holding Corporation	Public
Norbord Inc.	Private
Newfoundland and Labrador Hydro	Public
Newfoundland Power	Private
NOVA Chemicals Corporation	Private
Nova Scotia Power Inc.	Private
Ontario Power Authority	Public
Ontario Power Generation Inc.	Public
Petro-Canada	Private
PowerStream Inc.	Public
SaskEnergy Incorporated	Public
SaskPower	Public
SaskTel	Public
Siemens Power Generation	Private
Toronto Hydro Corporation	Public
Ultramar Ltée	Private
Vale Inco Limited	Private
Private	15
Public	15
Total	**30**

Using the above model for setting executive compensation, as recommended by the Agency Review Panel, results in reduced compensation for new executives.

Current Methodology

In December 2008, Hydro One decided to take these recommendations further than required by the Agency Review Panel. For the year 2009 and thereafter, Hydro One will apply the post-Agency Review Panel methodology to all current and new management employees in the company, including current and new executives and senior management, and accordingly will cease using the pre-Agency Review Panel methodology for employees who were executives prior to June 2007.

(2) Performance-Based Compensation

Our company does not grant to its executive officers any options, warrants or other rights to purchase its stock, including stock appreciation rights. Performance-based compensation is restricted to the Incentive Plan.

Hydro One's Incentive Plan is a mechanism used by the Company to drive performance, and is separate and distinct from base salary adjustments. The Incentive Plan is designed to establish a strong correlation between corporate performance, individual performance and at-risk compensation. Hydro One's Incentive Plan provides an opportunity for participants, including the NEOs, to earn an annual cash incentive payment based on two elements. The first element is the achievement of corporate performance targets set by the Board of Directors. The second element is the participant's contributions to these targets.

For the purposes of determining the amount of short term incentive payable to the President and Chief Executive Officer, specific weightings and levels of achievement are assigned to each corporate performance measure established by the HRPP Committee. In addition, other specific qualitative and leadership goals are also taken into account by the HRPP Committee. The assessment of the President and Chief Executive Officer is conducted by the HRPP Committee and approved by the Hydro One Board.

There are two components to performance-based compensation for NEOs other than the President and Chief Executive Officer: fund determination and fund allocation. These components will be described separately.

Fund Determination: The funds available for the direct reports of the President and Chief Executive Officer (which includes the NEOs other than the President and Chief Executive Officer) is a percentage of the total payout which would be payable assuming each individual earned his or her maximum allowable short term incentive. In 2008, the maximum percentage of funds available for the direct report population to the President and Chief Executive Officer was set at 75% of this total potential payout. This determination was made by the HRPP Committee of the Board, and recommended to the Board of Directors, by measuring the company's performance at the end of the year against various corporate performance targets and measures set at the beginning of the year. The maximum percentage for funding is at the discretion of the Hydro One Board of Directors, based on a recommendation by the HRPP Committee.

Fund Allocation: The fund is allocated among individual executives on the basis of performance. It is not an across the board allocation. NEOs are assessed against their performance agreement and against the rest of the direct report population, based on objective

and subjective assessments. These assessments of the NEOs, other than the President and Chief Executive Officer, are conducted by the President and Chief Executive Officer, and approved by the HRPP Committee. No direct report is allowed to receive above their maximum allowable short term incentive. A further discussion on the evaluation of performance of the NEOs is set out below in the section dealing with individual performance.

(a) Corporate Performance Measures and Targets

The HRPP Committee develops Hydro One's corporate performance measures and targets annually at the beginning of each year through the use of a balanced scorecard. A balanced scorecard is designed to measure corporate performance broadly, covering all key aspects of corporate performance. Measures included in the scorecard are designed to ensure that corporate productivity is enhanced and the corporate strategy is achieved.

The scorecard is intentionally not weighted. Each measure is key to driving corporate performance, and all of the measures are interrelated. In terms of assessing performance, the HRPP Committee is required to exercise judgement in weighing the results for each measure and determining whether overall corporate performance, as reflected through scorecard performance, is met. If, on balance, scorecard performance is met or exceeded, the short term incentive fund is funded to 75% of the maximum short term incentive payout. If, on balance, scorecard performance is not met, the HRPP Committee will determine a lesser funding level, somewhere between 0 and 75% of the maximum short term incentive fund, depending on performance.

In the fall of each year, Hydro One's management identifies the key measures and targets which it believes will drive corporate performance during the course of the following year and presents these recommended measures and targets to the HRPP Committee. Over the next few months, management and the HRPP Committee review, consider and assess the measures and targets to ensure they cover all key aspects of corporate performance and are robust enough to drive superior performance and corporate strategy implementation. Once satisfied, the HRPP Committee recommends the measures and targets to the full Board of Directors for approval. These measures and targets are based on Hydro One's key strategic goals in the areas of financial performance, transmission reliability, customer satisfaction, major projects, employees and safety and environment. Each of these strategic goals is discussed below.

1. Financial Performance

Achievement of strong financial performance is measured by our three performance measures of a strong credit rating, productivity achievements and high net income. In relation to our credit rating, Hydro One's long term credit ratings provided by Standard & Poor's, Moody's and DBRS met the targeted "A" rating category. During 2008, Standard & Poor's announced an increase in Hydro One's long term debt rating to "A+" from "A", and affirmed the "A-1" short-term rating of our company. The rating reflects a stable energy policy in Ontario and consistent, independent regulation. Maintaining an "A" category credit rating allows us to have access to long-tem debt markets on a cost-effective basis. In terms of productivity achievements, the productivity index is a composite indicator used to indicate productivity achievements. This index is composed of two measures from each of the six lines of business with the objective to achieve an average of 90% of the measures. The year end result exceeded our target. In relation to net income, our target was $440 million for 2008, and in fact was exceeded. Accordingly, Hydro One met all three of the performance measures within this strategic goal.

2. Transmission Reliability

Hydro One aims to retain and build public confidence and trust in our operations, as stewards of Ontario's electricity grid. In 2008, Hydro One continued its focus on this strategic priority by investing in the key assets of the electricity delivery system and by operating the existing system for customers in a safe, reliable and efficient fashion. Transmission reliability measures the frequency and duration of unplanned customer interruptions and compares the results of Hydro One's performance with other large sized participants of the Canadian Electricity Association ("CEA"). Reliability is influenced by weather patterns and generation constraints and accordingly to achieve results, Hydro One requires good performance from both its transmission and distribution systems. Hydro One is conscious that businesses of all sizes require a reliable service to allow them to deliver their products and services. In 2008, Hydro One targeted and achieved top quartile transmission reliability (as measured by frequency and by duration of unplanned customer interruptions) as compared to other large sized CEA participants. Additionally, Hydro One participated in a 2008 U.S. utility benchmarking study on reliability. The results confirmed that our transmission system is also top quartile compared with the U.S. transmission utilities. Accordingly, Hydro One met the two performance measures within this strategic goal.

3. Customer Satisfaction

Keeping customers satisfied is also an integral part of Hydro One's business focus. Customer satisfaction measures the degree to which our customers are satisfied with the service they receive from our company. Additionally, corporate reputation is a key influencer in customer satisfaction. As a result, Hydro One focused on improving reputation and our success in this area is demonstrable. Hydro One was honoured in the Top Ten list of Corporate Citizens and was ranked first among utilities. Customer satisfaction is measured based on the results of various customer surveys. In 2008, we targeted a customer satisfaction rate of 85% and achieved a customer satisfaction rate of 86%, thereby exceeding slightly the target. Results of this measure have steadily improved since 2003 when it was first introduced when our company achieved 61% customer satisfaction.

4. Major Projects

As the stewards of the province's electricity delivery system, Hydro One has a number of key investment initiatives and projects that require special attention. Accordingly, Hydro One identifies specific key projects each year and measures progress for each project against its project plan. In 2008, the following key projects were identified and each was targeted to be substantially on time and substantially on budget:

1) Interconnect with Hydro-Québec
2) Claireville TS – Gas Insulated Switchgear Replacement System
3) Bruce to Milton 500kV line
4) Enterprise information technology infrastructure replacement ("Cornerstone Project")

Hydro One met all four performance measures within this strategic goal, as each of the key projects was substantially on time and substantially on budget as compared to its project plan.

5. Employees

Hydro One's greatest assets are its employees. Accordingly, a number of metrics with respect to skills and safety training and development of Hydro One's management employees are measured.

With respect to employee development, including management employees, Hydro One believes that skills and safety training is a strong proxy for employee development. Accordingly, Hydro One measures the percentage of skills and safety training completed in any year compared to plan. During 2008, we continued to build on the strategic direction established by Hydro One management in 2007 ensuring that each line of business identified the necessary job competencies, training gaps, and developed the necessary training to close those gaps. In 2008, Hydro One targeted having 90% of its employees complete their required training during the year and achieved 94%, thereby exceeding this performance target.

6. Safety and Environment

With respect to safety, the potentially hazardous nature of Hydro One's business demands constant focus in this area. Hydro One measures the number of serious incidents involving its employees. Serious incidents refer to, among other things, electrical contacts, preventable motor vehicle accidents, work equipment failures, asset equipment failures, falling objects and falls to a different level. In 2008, Hydro One targeted less than 4.5 serious incidents reported per million hours worked. Hydro One achieved a better than target result of 3.6 serious incidents per million hours worked. However, in order to reflect that the serious incidents that occurred in 2008 included a fatality, the HRPP Committee agreed with management that this target had not been met.

Hydro One tracks its percentage completion of environmental project milestones, including the site remediation clean-up plan for the 2008 Land Assessment Remediation program, conducting energy audits at two additional owned facilities, the implementation of energy audit recommendations at three locations, the light duty vehicle replacement program, the energy efficiency and environmental design for a new service centre, and the installation of GPS Telematics units in 500 vehicles and remedial actions to reduce CO2 emissions and improve vehicle utilisation. The achievement of these milestones demonstrates our company's commitment to becoming a leader in implementing environmentally-sustainable solutions. Hydro One exceeded the established target for 2008.

7. Overall Performance for 2008

For 2008, the HRPP Committee determined that of the 18 corporate targets, 2 were exceeded, 15 were met and one was missed due to an employee fatality. The HRPP Committee determined, by reason of a balanced scorecard assessment, that this level of achievement supported the establishment of payout funding at 75% of the maximum allowable short term incentive for the direct reports of the President and Chief Executive Officer, which include the NEOs other than the President and Chief Executive Officer. The 75% funding of the maximum allowable short term incentive applied to all management employees, including the NEOs.

(b) Individual Performance

The second component of determining the amount of short term incentive payments to be made to NEOs pursuant to the Incentive Plan is their individual performance. Individual target

performance criteria are outlined in individual performance agreements which include both broad corporate and individual specific targets. NEOs are expected to align their efforts with and advance the Corporate Performance Measures and Targets discussed above. In addition, the following leadership attributes are factored into individual performance targets: communicates vision and purpose, deals with ambiguity, builds customer and stakeholder support, lives the values, possesses business acumen, sets priorities, has managerial courage, drives for results, is a team player, and develops staff capability. Performance agreements are entered into annually between the President and Chief Executive Officer and her direct reports. The Board of Directors, in turn, annually approves the performance agreement entered into between the President and Chief Executive Officer and the Chair of the Board.

Potential awards for NEOs are expressed as a percentage of base salary. For each of the NEOs, potential awards range between 0% and a maximum of 60% of base salary. For the year ended December 31, 2008, the potential awards ranges for the NEOs were as follows: between 0% and 25% of base salary for Ms. Formusa, and between 0% and 60% of base salary for each of Ms. Summers, Mr. D'Arcey, Mr. Goldie, and Mr. McQueen. Awards are granted on the basis of individual performance against the measures and targets in the performance agreements, individual performance relative to other senior executives and within the context of a 75% of maximum potential payout amongst the direct report population to the President and Chief Executive Officer.

In 2008, 50% of the 2008 Incentive Plan payout for each NEO was based on meeting specific targets related to the company's major information technology and business transformation initiative, a project above referred to as Cornerstone. The following three Cornerstone specific measures had to be met for the NEOs to receive the 50% portion for Cornerstone. Otherwise, the payout for this portion would be zero.

- the project must be substantially on time and on budget at year end;
- all 2008 project milestones must be substantially achieved; and
- each NEO must remain committed to the successful completion of the project and work collegially to ensure its success.

Each of these challenging targets was met.

The remainder of the potential award for each NEO was based on his or her relative achievement of specific individual performance targets. As noted earlier, these targets may be objective, numeric-based targets or more subjective targets. These targets are linked to some or all of the corporate performance measures and the NEO's business unit and were designed to enable our company to achieve its five year vision: ensuring public confidence as stewards of provincial assets, best safety record, top quartile transmission and distribution reliability, 90% customer satisfaction, skills development and retention of employees, and shareholder returns. The evaluation of performance against the targets is important. Hydro One does not take a mechanistic approach to assessment. Each NEO is assessed objectively against his/her specific individual targets. Once this assessment has been completed, a second assessment comparing relative achievement across the NEOs is also conducted. This approach requires judgment on the part of the President and Chief Executive Officer (with respect to the NEOs other than the President and Chief Executive Officer) and the HRPP Committee of the Board (with respect to the President and Chief Executive Officer), but provides a better assessment of performance since it considers both absolute performance (against a set of targets) and relative performance against the other NEOs (other than the President and Chief Executive Officer). Using this

approach means an NEO could meet all of his/her targets but receive significantly less than his/her incentive maximum if other NEOs performed better against their targets.

Ms. Formusa's targets were both quantitative (weighted) and qualitative. The quantitative factors were financial (40%), transmission reliability and customer satisfaction (20%), four major projects (20%) and employee, safety and the environment (20%). The financial target related to our company's performance, reflected in maintaining its "A" credit rating category, as well as productivity improvements and achieving net income. The transmission reliability and customer satisfaction target focused on frequency and duration of unplanned customer interruptions, which can impact on customer satisfaction. Four major projects with significant implications for our company (Claireville TS, Hydro-Québec Interconnect, Bruce to Milton and Cornerstone) were chosen and their progress against plan and budget were measured. In the area of employee, safety and the environment, targets were set to measure skills, safety training and development of employees and to reduce serious injuries and our company's footprint on the environment. Finally, qualitative factors were identified, including leadership, culture, Board and stakeholder relationships, employee focus and stability, the development of successors for the Chief Executive Officer position and compliance with corporate policies.

Ms. Summers' targets were aimed at reinforcing compliance in the company and throughout the finance function, achieving benefits from the strategic sourcing organization to reduce materials costs, successfully completing the 2008 debt program, maintaining the pension fund's position when measured against other Canadian pension plans, implementing the Cornerstone enablement organization, and completing staffing and succession plans for finance and supply chain. Ms. Summers targets also addressed increasing productivity and continuous improvement, preparing our company for the introduction of International Financial Reporting Standards, and transitioning the company to the new external auditors.

Mr. D'Arcey's targets were focused on initiatives in the areas of safety and customer satisfaction, including focus on individual/team accountability to achieve zero serious injuries and reduced high-rated incidents, delivering the customer benefits of improved scheduling, and improving call center call handling and bad debt management. Mr. D'Arcey targets also included successfully deploying the smart meter program, completing the forestry program and asset condition assessment programs to improve system reliability. Mr. D'Arcey's was also to identify or secure succession candidates for the Customer Operations group and for his position, in particular. In his role as President and Chief Executive Officer of Hydro One Remote Communities Inc., Mr. D'Arcey delivered upon the 2008 Remote Communities scorecard objectives of financial strength, customer loyalty and relationships, system reliability, workforce health and safety and the associated performance measures related to those objectives.

Mr. Goldie's targets included a number of initiatives with respect to the human resources function, including the negotiation of a collective agreement with one of our company's unions, integration of the Organization Alignment (change management) function within the lines of business, implementation of a candidate assessment program for apprenticeship hiring, and initiation of a program for knowledge retention and transfer. Mr. Goldie's targets also addressed the development of a company-wide employee engagement survey, successfully chairing the Human Resources Committee of the Canadian Electricity Association on behalf of Hydro One, as well as chairing the Electricity Sector Council and ensuring it met its strategic goals for 2008, and developing succession plans for all key positions in Corporate Services. With respect to

information technology targets, Mr. Goldie was to undertake the Network Management System replacement strategy and improve the business relationship with the company's external provider, Inergi LP. From a corporate security perspective, targets included achieving implementation of the new Theft of Copper Program and achieving cost savings/investment in that program.

Mr. McQueen's initiatives were focused on the sustainment and development of our company's assets to deliver on the objectives of reliability, customer satisfaction and stewardship of assets. Mr. McQueen's targets were to ensure that major projects were delivered substantially on time and on budget, deliver the 2008 planned work program, develop effective Engineering & Construction Services (E&CS) measures to ensure that all E&CS actions necessary to enable the full Cornerstone benefits to be achieved are implemented, and to develop succession plans for all key senior positions in E&CS.

In 2008, all NEOs substantially met all of their specific individual performance targets resulting in incentive payments that ranged from approximately 68% to 100% of the maximum award available based on a subjective assessment of relative performance compared to other NEOs in their performance against their respective targets and subject to the overall cap on funding equal to 75% of the maximum potential payout amongst the direct report population to the President and Chief Executive Officer.

Stewardship is a key corporate value of Hydro One. As such, it is important that the NEOs demonstrate compliance with Hydro One's policies and procedures. To demonstrate stewardship on prudent financial responsibility, a compliance target of 95% for each NEO's organization was set with respect to corporate credit card transactions. If these compliance targets were not achieved, the NEO's Incentive Plan award would be reduced by 25%. Each of the NEOs achieved these targets.

The determination of Incentive Plan amounts for the NEOs is independent from the assessment of base salary adjustments. However, the final dollar amount of an annual Incentive Plan payment is impacted by any changes to base salary since it is a percentage of base salary.

(3) Benefits

In addition to the Base Salary and Performance Based Compensation, as part of their compensation package, the NEOs also participate in the Hydro One registered pension plan and supplementary pension plan and participate in a flexible benefits plan, which is available to all other management employees. The flexible benefits plan provides various benefits, including life insurance, long term disability benefits, accident insurance, vacation and extended health care benefits. Hydro One provides to each executive and management employee certain core benefits, which include basic life insurance, accidental insurance, extended health benefits, out of country medical dental, sick leave and long term disability, pension and basic vacation. Additionally, senior management has the option of receiving a third-party medical assessment. The flexible benefit plan provides for credits calculated each plan year on the individual's base annual earnings in effect at the time of enrolment in the plan. Those flexible benefit plan credits may then be allocated by each executive and management employee to additional life insurance, additional vacation (where applicable), a health care and/or general benefits account. Unallocated credits are paid out at year end, subject to withholding tax, to the employee.

Benefits provided to NEOs are the same as those provided to all other management employees, with the exception of financial counselling and third-party medical assessment, and could be higher or lower than bargaining unit represented staff, depending on the specific benefit. Benefits are relatively independent of base salary and Incentive Plan payments, although some are a percentage of base pay. Many health-related benefits are a flat rate and not related to base salary or Incentive Plan levels

Pension benefits for NEOs are identical to those of all other executive and management staff in our company with the same start date, and are calculated in a similar manner identical to all employees in our company. See "Pension Plan Benefits" below.

NEOs do not have any perquisites and personal benefits which other executive and/or management staff does not receive. Perquisites and benefits generally follow those negotiated by bargaining units in the company, although the NEOs benefits have not kept pace in some areas with those of bargaining unit represented employees.

Role of NEOs in Determining Executive Compensation

An NEO does not play any part in determining his or her own compensation. The Senior Vice President - Corporate Services, working with staff and Hay Management Consultants, a compensation consultant, is responsible for providing recommendations to the HRPP Committee consistent with the Board approved compensation strategy. The HRPP Committee must then review, discuss, and ultimately approve the base salary, Incentive Plan payment and benefits for the NEOs (other than the President and Chief Executive Officer) based on a recommendation by the President and Chief Executive Officer. With respect to the compensation payable to the President and Chief Executive Officer, the HRPP Committee reviews, discusses and makes a recommendation to the Board of Directors, who must consider, discuss and ultimately approve the final compensation level for the President and Chief Executive Officer.

Summary Compensation Table

The following table summarizes the compensation paid in 2008 to each of the Chief Executive Officer, Chief Financial Officer and to each of the three other most highly compensated executive officers.

Name and Principal Position	Year	Salary ($)	Share-based awards ($)	Option-based awards ($)	Non-equity incentive plan compensation ($)		Pension Value ($)	All Other Compensation ($)	Total Compensation ($)
					Annual incentive plans[1]	Long-term incentive plans			
L. Formusa President & CEO	2008	$725,000	$0	$0	$170,375	$0	$241,000		$1,136,375

B. Summers Executive Vice President and CFO	2008	$386,280	$0	$0	$231,768	$0	$105,000	$723,048
M. D'Arcey Senior Vice President, Customer Operations	2008	$334,000	$0	$0	$175,000	$0	$105,000	$614,000
T. Goldie Senior Vice President, Corporate Services	2008	$321,000	$0	$0	$145,000	$0	$83,000	$549,000
N. McQueen Vice President, Engineering & Construction Services	2008	$293,000	$0	$0	$120,000	$0	$94,000	$507,000

[1] Information in the Summary Compensation Table is based on the year the incentive was earned. The incentive is generally earned in one year and paid in the following year. Therefore, the information provided in the Summary Compensation Table below differs from that published under the Public Sector Salary Disclosure Act (Ontario) for the year ended December 31, 2008.

None of Ms. Formusa, Ms. Summers, Mr. D'Arcey, Mr. Goldie or Mr. McQueen are entitled to other benefits or perquisites in the aggregate amount that exceeds $50,000 or 10% of the total of his or her annual salary or incentive payment.

Ms. Formusa does not receive any additional compensation for her services as a Director of Hydro One.

Pension Plan Benefits

Defined Benefit Pension Plan

Hydro One provides a defined benefit pension plan to its employees. Each of the NEOs participates in the Hydro One Pension Plan (consisting of the Hydro One registered pension plan and the supplementary pension plan). The benefits for these individuals are calculated in a consistent manner with all other Hydro One employees, as described below.

For each year of credited service under the Hydro One Pension Plan, to a maximum of 35 years, the benefit provided for each of the employees who participate in the plan is equal to 2% of the member's average base annual earnings during the 36 consecutive months (60 consecutive months for management employees hired on or after January 1, 2004 and for employees represented by the Society of Energy Professionals hired on or after November 17, 2005) when his or her base annual earnings were highest. Base annual earnings are comprised of the member's salary and 50% of his or her short term incentive, if applicable.

The approximate projected credited years of service that each NEO will have if he or she works until the age of 65 is as follows: Ms. Formusa – 35 years at age 65; Ms. Summers – 34 years at age 65; Mr. D'Arcey – 35 years at age 65; Mr. Goldie – 35 years at age 65; and Mr. McQueen 15 years at age 65.

This pension is reduced by 0.625% of the member's average base annual earnings up to the year's maximum pensionable earnings during the 36 consecutive months (60 consecutive months for management employees hired after January 1, 2004 and for employees represented by the Society of Energy Professionals who were hired after November 17, 2005) when his or her base earnings were highest (the reduction is 0.500% for employees represented by the Society of Energy Professionals who were hired prior to November 17, 2005 and for all employees represented by the Power Workers' Union). The reduction is intended to offset Canada Pension Plan ("CPP") benefits.

The plan terms also include a bridge pension which is payable from the date of retirement to age 65 for all members except for management employees hired on or after January 1, 2004 and employees represented by the Society of Energy Professionals hired on or after November 17, 2005. The Hydro One Pension Plan provides for early retirement with an unreduced pension at the earlier of age 65 and the attainment of years of age plus continuous employment totalling 82 or more (85 years of age plus credited service for management employees hired on or after January 1, 2004 and for employees represented by the Society of Energy Professionals hired on or after November 17, 2005). A plan member who is not eligible for an unreduced pension can retire with a reduced pension any time after attaining age 55.

Pension benefits payable to pensioners, beneficiaries and terminated employees with deferred pensions are increased annually effective January 1 of each year equal to 100% of the increase in the Ontario consumer price index for the 12 month period ending in June of the previous year (75% for management employees hired on or after January 1, 2004 and for employees represented by the Society of Energy Professionals hired on or after November 17, 2005). The normal form of pension for a member who does not have a spouse at retirement is a pension payable for life and guaranteed for five years, payable to an estate if not paid to the retiree. The normal form of pension for a member who has a spouse at retirement is a pension payable for the life of the member, and continuing after the member's death to his or her spouse at the rate of 66 2/3% of the amount the member was receiving.

Benefits payable under Hydro One's registered pension plan, similar to other entities, are restricted by the *Income Tax Act* (Canada). This limit on benefits affects members whose average annual earnings exceed approximately $130,000 in 2008. Participants whose pensions would otherwise be restricted by the *Income Tax Act* (Canada) participate in an unregistered supplementary pension plan that provides benefits equal to the difference between the *Income Tax Act* (Canada) maximum pension benefits and the benefits determined in accordance with the formula set out in Hydro One's registered pension plan. The supplementary pension plan is unfunded and the additional retirement income is paid from general revenues. Hydro One's obligations to participants under the supplementary pension plan are secured by a letter of credit.

The table below shows the following information for each NEO participating in Hydro One's defined benefit pension arrangements:

- Years of credited service as at December 31, 2008 and as at the normal retirement age of 65;

- Estimated annual benefit accrued, or earned, for service up to December 31, 2008 and up to the normal retirement age of 65; and
- A reconciliation of the accrued obligation from December 31, 2007 to December 31, 2008. The accrued obligations reflect the impact of the annual bonus earned in the year even though it is paid in the following year.

Name	Number of years credited service at year end (#)	Annual benefits payable ($)		Accrued obligation at start of year [1] ($)	Compensatory change [2] ($)	Non-compensatory change [3] ($)	Accrued obligation at year end [4] ($)
		At year end	At age 65				
L. Formusa	27.9 yrs	$285,700	$358,200	$6,268,000	$241,000	($1,303,000)	$5,206,000
B. Summers	7.8 yrs	$65,600	$286,200	$670,000	$105,000	($319,000)	$456,000
M. D'Arcey	30.2 yrs	$231,000	$268,100	$3,876,000	$105,000	($976,000)	$3,005,000
T. Goldie	30.9 yrs	$227,000	$257,200	$3,885,000	$83,000	($901,000)	$3,067,000
N. McQueen	8.6 yrs	$53,700	$94,400	$681,000	$94,000	($165,000)	$610,000

[1] The accrued obligation is the value of the projected pension earned for service to December 31, 2007. The values have been determined using the same actuarial assumptions used for determining the pension plan obligations at December 31, 2007 as disclosed in the notes to the 2007 consolidated financial statements, based on actual earnings for 2007 and adjusted to reflect expected increases in pensionable earnings.

[2] The values shown under the column headed Compensatory Change include the value of the projected pension earned for service in the year (reduced by the NEO's own contributions) plus the differences between actual and assumed compensation for the year.

[3] The values shown under the column headed Non-Compensatory Change include the impact of amounts attributable to interest accruing on the beginning-of-year obligation, changes in the actuarial assumptions, the NEO's own contributions and any other experience gains and losses.

[4] The accrued obligation is the value of the projected pension earned for service to December 31, 2008. The values have been determined using the same actuarial assumptions used for determining the pension plan obligations at December 31, 2008 as disclosed in the notes to the 2008 consolidated financial statements, based on the actual earnings for 2008 and adjusted to reflect expected increases in pensionable earnings.

Notes:

- All members are currently vested in their pension entitlements earned to December 31, 2008.
- In accordance with Canadian generally accepted accounting principles, the amounts above make no allowance for the different tax treatment of the portion of pension not paid from the registered or qualified pension plans.
- All amounts shown above are estimated based on assumptions and represent contractual entitlements that may change over time.

The method and assumptions used to determine estimated amounts will not be identical to the method and assumptions used by other issuers and, as a result, the figures may not be directly comparable across issuers.

Termination and Change of Control Benefits

Each of Ms. Formusa, Ms. Summers, Mr. Goldie, Mr. McQueen and Mr. D'Arcey is a party to an employment agreement with Hydro One governing the terms of their employment. None of the NEOs have any rights or receive benefits on a change of control of the company. With respect to Ms. Formusa, Ms. Summers, Mr. Goldie, Mr. McQueen, and Mr. D'Arcey, if their employment is terminated by Hydro One without cause, each of Ms. Formusa, Ms. Summers, Mr. Goldie, Mr. McQueen, and Mr. D'Arcey is entitled to receive an amount equal to her or his base salary at the date of termination in equal monthly instalments (or in the case of Ms. Summers, in one lump sum) for a period of 24 months (18 months in the case of Mr. McQueen) and to receive benefits over the same period (including incentive plan payments equal to the average of the three previous incentive plan payments). Each of Ms. Formusa, Ms. Summers, Mr. Goldie Mr. McQueen and Mr. D'Arcey would continue to earn credited service under the Hydro One Pension Plan during such 24-month period (18-month period in the case of Mr. McQueen).

The amount of salary and incentive plan payments expected to be paid if Ms. Formusa's employment were terminated on December 31, 2008 total $1,722,800. Ms. Formusa's annual pension accrued at December 31, 2008 is also expected to increase by $180,300.

For Ms. Summers, the amount of salary and incentive plan payments expected to be paid if her employment were terminated on December 31, 2008 total $1,095,893. Ms. Summers' annual pension accrued at December 31, 2008 is also expected to increase by $24,000.

Regarding Mr. D'Arcey, if his employment was terminated on December 31, 2008, the amount of salary and incentive plan payments expected to be paid would total $966,333. Mr. D'Arcey's annual pension accrued at December 31, 2008 is also expected to increase by $23,400.

In respect of Mr. Goldie, the amount of salary and incentive plan payments expected to be paid if Mr. Goldie's employment were terminated on December 31, 2008 total $922,000. Mr. Goldie's annual pension accrued at December 31, 2008 is also expected to increase by $21,500.

As for Mr. McQueen, the amount of salary and incentive plan payments expected to be paid if his employment was terminated on December 31, 2008 total $591,988. Mr. McQueen's annual pension accrued at December 31, 2008 is also expected to increase by $12,400.

The payment levels have been determined based on standard factors considered in termination situations, such as age, length of service, proximity to retirement and job level.

Ms. Formusa, Ms. Summers, Mr. Goldie, Mr. McQueen and Mr. D'Arcey are not entitled to receive any payment in the event of termination for cause or voluntary termination.

Upon retirement, all NEOs are entitled to benefits, which include core health and dental coverage and life insurance applicable to all management employees employed at Hydro One. These benefits are identical to the benefits provided to other management employees in the company. No additional benefits are provided in the NEO's employment contract.

For the NEOs, there are no significant conditions or obligations that apply to receiving any of these benefits or payments other than a standard company confidentiality agreement.

Director Compensation

The by-laws of Hydro One provide that directors may receive reasonable remuneration for their services, commensurate with their duties, together with reimbursement for all reasonable expenses incurred in fulfilment of their duties, including travel expenses. The amount of such remuneration is determined by the Board of Directors from time to time. The following remuneration is currently paid to directors:

Retainer for directors	$25,000 per annum
Retainer for Committee Chairs	$3,000 per annum
Participation in Board and Committee Meetings	$900 per meeting

The fees are reviewed periodically but have not been revised since 2001. The President and Chief Executive Officer is not entitled to these fees.

Directors' fees, less statutory deductions, are paid quarterly by direct deposit or cheque as requested.

On March 31, 2008, Rita Burak resigned as Chair of the Board of Directors and James Arnett was appointed Chair of the Board of Directors. Douglas Speers was appointed as Chair of our Board of Directors, on an interim basis, on December 8, 2008, following the appointment of James Arnett as Special Advisor to the Government of Ontario on the auto sector's restructuring plans. Mr. Arnett was re-appointed as Chair of the Board of Directors effective February 17, 2009. The Chair receives annual remuneration of $150,000 per annum and does not receive any additional fees for serving as a director.

The following table summarizes the compensation paid in 2008 to the directors of Hydro One.

DIRECTOR COMPENSATION TABLE

Name	Fees earned ($)	Total ($)

Rita Burak	$37,500.00	$37,500.00
(Chair – January 1 to March 31, 2008)	(Jan.1 to Mar. 31)	
James Arnett	$103,260.87	$103,260.87
(Chair – March 31 to December 8, 2008)	(Apr. 1 to Dec. 8)	
Douglas Speers	$65,180.93	$65,180.93
(Chair – December 8 to December 31, 2008, Director January 1 to December 8, 2008)	(Dec. 9 to Dec. 31)	
Sami Bébawi	$50,501.46	$50,501.46
Kathryn Bouey	$51,101.46	$51,101.46
Murray Elston	$55,901.46	$55,901.46
Don MacKinnon	$46,001.46	$46,001.46
Michael Mueller	$58,601.46	$58,601.46
Walter Murray	$64,001.46	$64,001.46
Robert Pace	$53,801.46	$53,801.46
Gale Rubenstein	$43,001.46	$43,001.46

* Laura Formusa does not receive compensation as a director.

Independent Advice

The Committee engages the services of an independent consultant from the Hay Group to provide advice and counsel on compensation matters, including executive compensation. During 2008, the Hay Group was paid an aggregate of $41,027.04 for their advice.

In December 2008, the Committee also engaged the services of Hugessen Consulting Inc. to provide advice on the competitiveness and effectiveness of the Company's compensation programs. As of year end, Hugesson Consulting Inc. was paid an aggregate of $23,703.75 for their advice.

APPOINTMENT OF AUDITOR

On December 13, 2007, the board of directors recommended to our sole shareholder that KPMG LLP be appointed as the auditor of our company for the fiscal year ended December 31, 2008. This appointment was confirmed by our sole shareholder on December 18, 2007. Ernst & Young LLP, the auditor of our company for the fiscal year ended December 31, 2007, was first appointed as auditor on January 18, 1999.

AUDIT AND FINANCE COMMITTEE INFORMATION

The Audit and Finance Committee's Charter

Our Audit and Finance Committee's mandate is attached hereto as Appendix "A", which Appendix is hereby incorporated by reference. Appendix "A" reflects the Audit and Finance Committee mandate effective February 13, 2008.

Composition of the Audit and Finance Committee

As at December 31, 2008, the members of our Audit and Finance Committee were Walter Murray, Murray J. Elston, Michael Mueller and Robert Pace. All members are independent and financially literate as such terms are defined under applicable Canadian securities legislation.

Relevant Education and Experience

In addition to each member's general business experience, the education and experience of each Audit and Finance Committee member that is relevant to the performance of his or her responsibilities as an Audit and Finance Committee member is described below.

Mr. Murray is the former Vice-Chairman and member of the Executive Committee of RBC Capital Markets, an international corporate and investment bank. His 38 year career at the RBC Royal Bank included Senior Executive Investment Banking responsibility, Executive head of corporate banking activities for Canada and Regional Executive for RBC's Midwestern USA Corporate Banking operations. Since 2000, Mr. Murray has been a director of Ivernia Inc.'s Board of Directors and Chair of its audit committee. Mr. Murray holds a Bachelor of Commerce degree from Concordia University majoring in Accounting and Business Administration. He is

also a graduate of the Executive Development Program at the Tuck School of Business, Dartmouth University, New Hampshire.

Mr. Elston has held various senior positions in the Government of Ontario including Chairman of the Management Board, Chairman of the Public Accounts Committee and Minister of Financial Institutions which involved a regulatory function with respect to financial institutions. Mr. Elston has also served in officer positions of several non-profit companies.

Mr. Mueller is a former Global Leader of PricewaterhouseCoopers' (PwC) Private Company Services/Middle Market Practice and a former member of PwC's Global Audit Leadership Team, Global Advisory Leadership Team and the Global Markets Council. Mr. Mueller is a Chartered Accountant, a Certified Insolvency Practitioner and a Chartered Business Valuator.

Mr. Pace is President and Chief Executive Officer, The Pace Group Ltd., which owns and operates a number of companies across Atlantic Canada. He serves on the Board of Directors of Canadian National Railway Company and is the former chair of its audit committee. He also serves on the audit committee of High Liner Foods Incorporated and Overland Realty Limited. Mr. Pace holds both a Bachelor of Laws and a Masters in Business Administration degree from Dalhousie University. He has completed a corporate director education program at Harvard Business School relating to compensation committees, and a corporate director education course at the Chicago Business School, Stanford Law School and The Wharton Business School (Joint Offering) relating to corporate governance.

Audit and Finance Committee Oversight

There have been no recommendations of our Audit and Finance Committee to nominate or compensate an external auditor which have not been adopted by our Board of Directors.

Pre-Approval Policies and Procedures

In accordance with the provisions of its mandate, the Audit and Finance Committee ratifies all non-audit services, as pre-approved by the Committee Chair, to be provided to our company by its external auditor.

External Auditor Service Fees

(a) *Audit Fees*

For fiscal 2008, Hydro One changed its external auditor from Ernst & Young LLP to KPMG LLP. The audit fees to be billed by KPMG LLP for fiscal 2008 are estimated to be $881,300. The audit fees billed by Ernst & Young LLP for fiscal 2007 were $857,400.

(b) *Audit-Related Fees*

The total audit-related fees billed by KPMG LLP for fiscal 2008 are estimated to be $140,000. The nature of services rendered were: audit of the Hydro One Pension Plan, French translations and executive expense reviews. Prospectus

related activities were included audit fees by KPMG LLP for fiscal 2008 but were reported as audit-related fees by Ernst & Young LLP for fiscal 2007.

The audit-related fees billed by Ernst & Young LLP for fiscal 2007 were $185,400. The nature of the services rendered were: audit of the Hydro One Pension Plan, French translations, executive expense reviews and prospectus related activities.

(c) *Tax Fees*

There were no tax fees billed by KPMG LLP for fiscal 2008.

The tax fees billed by Ernst & Young LLP for fiscal 2007 were $500. The nature of the services rendered were: general tax advice.

(d) *All Other Fees*

All other fees to be billed by KPMG LLP for fiscal 2008 are estimated to be $30,000 for ancilliary services. For fiscal 2007 all other fees billed by Ernst & Young LLP were $277,700 for information systems restructuring.

CORPORATE GOVERNANCE DISCLOSURE

Board of Directors

The Board of Directors of our company (the "Board") has undertaken an independence assessment and determined that, except as noted below, all of Hydro One's current directors are "independent" within the meaning of the rules adopted by the Canadian Securities Administrators (the "CSA"). Ms. Laura Formusa, who is the President and Chief Executive Officer of our company and a member of Board of Directors, is not independent.

The Board has separated the roles of Chair and Chief Executive Officer. Mr. Douglas Speers was appointed Chair of the Board on December 8, 2008 and is an independent director. The prime responsibility of the Chair of the Board of Directors is to provide leadership to the Board and to enhance Board effectiveness. The Chair, as the presiding member of the Board, also ensures that the relationships between the Board, management, the shareholder and other stakeholders are effective, efficient and further the best interests of our company.

Independent directors hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance. During 2008, seven such sessions without management were held. As well, the Audit and Finance Committee regularly holds such sessions with the external auditors and with the internal auditor. The Chair of the Audit and Finance Committee meets four times a year with the internal auditor. These sessions encourage open and candid discussion among the independent directors.

Summary of Attendance of Directors

The following table summarises the attendance of individual directors at meetings of the Board of Directors held for the 12-month period ending December 31, 2008.

Director	Board Meetings Attended
Douglas Speers	11 of 11
James Arnett[2]	8 of 8
Rita Burak[3]	2 of 2
Sami Bébawi	9 of 11
Kathryn Bouey	11 of 11
Murray J. Elston	11 of 11
Laura Formusa	11 of 11
Don MacKinnon[1]	10 of 10
Michael Mueller	11 of 11
Walter Murray	11 of 11
Robert Pace	11 of 11
Gale Rubenstein	10 of 11

(1) Mr. Don MacKinnon was not in attendance at one (1) Board Meeting because this meeting solely addressed a labour relations matter and, as President of the Power Workers' Union, he did not attend.

(2) Mr. James Arnett was appointed Chair of the Board of Directors of Hydro One Inc. on March 31, 2008 and he resigned on December 8, 2008. There were eight (8) meetings of the Board during that time. Mr. Arnett was re-appointed on February 17, 2009.

(3) Ms. Rita Burak resigned as Chair of the Board of Directors of Hydro One Inc. on March 31, 2008. There were two (2) meetings of the Board of Directors in 2008 prior to her resignation.

Directors' Board Memberships in Other Reporting Issuers

Director	Reporting Issuer
Walter Murray	Ivernia Inc.
Robert Pace	Canadian National Railway Company, Overland Realty Limited, High Liner Foods Incorporated

Board Mandate

The Board is responsible for the stewardship of our company and the supervision of management of the business and affairs of our company. The Board's accountabilities and responsibilities include development of our company's approach to corporate governance, the adoption of a strategic plan and the identification of the principal risks of our company's business. The Board

has adopted a written mandate, the text of which is set out as Appendix "B", which Appendix is hereby incorporated by reference.

Position Descriptions

The Board has adopted formal position descriptions for the Chair of the Board and the Board Committee Chairs. The position descriptions of each Committee Chair are set out in the Committees' mandates. In general, Committee Chairs are responsible for the leadership of their Committee as well as reporting to the Board on behalf of the Committee. The Board of Directors has also adopted a position description for the President and Chief Executive Officer, which sets out the key roles and responsibilities for that position.

Committees of the Board of Directors

The Board has established five standing committees of the Board and one ad hoc advisory committee of the Board and delegates certain of its enumerated responsibilities to each of the Committees. Notwithstanding this delegation, the Board retains its oversight function and ultimate responsibility for all matters delegated to committees.

The five standing committees of the Board are the Audit and Finance Committee, the Corporate Governance Committee, the Human Resources and Public Policy Committee, the Regulatory and Environment Committee and the Health and Safety Committee. The ad hoc advisory committee of the Board is the Business Transformation Committee. The roles and responsibilities of each Committee are set out in formal written mandates. These mandates are reviewed at least annually to ensure that they reflect best practices as well as applicable regulatory requirements. A brief summary of each of the Committees' responsibilities follows.

Audit and Finance Committee

The Audit and Finance Committee is composed entirely of independent directors as required by the Canadian Securities Administrators rules (for more information, see the mandate of the Audit and Finance Committee which is attached). The Audit and Finance Committee oversees the integrity of accounting policies and financial reporting, internal controls, internal audit, significant corporate risk exposures, financial compliance and ethics policies.

Corporate Governance Committee

The Corporate Governance Committee is composed entirely of independent directors. The Corporate Governance Committee acts as the nominating committee of the Board and recommends director candidates, committee assignments, director compensation, and corporate governance policy for committees and the board as a whole. The Corporate Governance Committee reviews the general and specific criteria applicable to candidates to be considered for nomination to the Board. The objective of this review is to maintain the composition of the Board in a way that provides the best mix of skills and experience to guide the long-term strategy and ongoing business operations of our company. In addition, the Corporate Governance Committee leads an annual evaluation of the Board and makes recommendations on modifications of the evaluation process.

Human Resources and Public Policy Committee

The Human Resources and Public Policy Committee (the "HRPP Committee") is composed entirely of independent directors. The HRPP Committee recommends compensation policy for senior managers, leads the performance review of the President and Chief Executive Officer, recommends bargaining strategy with respect to the unions, and advises the Board on public policy matters and corporate social responsibility issues. In this regard, the Committee also reviews succession planning and the recommendations for the appointment of persons to senior executive positions. In 2008, Hay Group were retained to review and provide advice on management compensation Also in December 2008, the HRPP Committee engaged Hugessen Consulting Inc. to advise the Committee and the Board on the competitiveness and effectiveness of the Company's compensation programs. For additional information relating to the compensation of our company's senior executives, see "Statement of Executive Compensation."

Regulatory and Environment Committee

The Regulatory and Environment Committee monitors our company's compliance with regulatory and environmental requirements and related risk, reviews related policies and generally oversees processes and procedures related to regulatory and environmental compliance at our company.

Health and Safety Committee

The Health and Safety Committee advises the Board on health and safety policies and standards, oversees compliance with health and safety regulations at our company, and reviews and reports to the Board on our company's emergency preparedness.

Business Transformation Committee

The Business Transformation Committee is composed entirely of independent directors and was established as an ad hoc advisory Committee of the Board specifically to assist the Board in its oversight responsibility on matters related to our company's Enterprise Application Systems Replacement Strategy.

The Enterprise Application Systems Replacement Strategy is a strategy to replace our existing customized business applications with commercially available software system applications to simplify our information technology infrastructure and improve the functionality of our business processes.

Orientation and Continuing Education

In 2008, Hydro One's Director Education Program was formalized in a written document, "The Director Orientation and Continuing Education Program", which was established in accordance with the principles set out in the *Business Corporations* Act (Ontario), National Policy 58-201: *Corporate Governance* Guidelines, the mandate of the Board and the mandates of the Corporate Governance and Audit and Finance Committees. The Director Orientation and Continuing Education Program consists of two elements: the New Director Orientation Program and the Continuing Director Education Program. The New Director Orientation Program consists of a Hydro One Directors' Guide, which is given to all new directors upon joining the Board to

provide them with an overview of the key organizational, financial, regulatory, and operational aspects of our company. The Directors Guide also contains information on the structure of the Board and its committees, committee mandates and general information on a director's obligations. In addition, new directors receive orientation sessions with the Chair, the President and Chief Executive Officer and members of the senior management team as well as tours of our company's facilities. The orientation sessions familiarize directors with Hydro One's strategic plans, its significant financial, accounting and risk management issues, its compliance programs, its Pension Plan and the directors' obligations as plan fiduciaries, and its Code of Business Conduct.

The Continuing Director Education Program includes, on an on-going basis, as part of regular Board meetings, information briefings, presentations and updates from senior management on relevant topics related to our company's business. These information items are either suggested by management or may be requested by members of the Board. As well, directors receive information from management in response to any actions arising at a board meeting or otherwise. The Continuing Director Education Program also includes articles and other information from relevant publications, which are forwarded to directors, visits to Hydro One facilities, and, attendance at industry events and conferences and seminars which are relevant external education opportunities or general courses of interest.

Ethical Business Conduct

The Board has adopted a written Code of Business Conduct (the "Code"). The Code sets out a comprehensive set of principles and expectations relating to ethical conduct, conflicts of interest and compliance with laws. The Code is part of Hydro One's internal control framework and applies to all of Hydro One's directors, officers and employees. The Code also applies to Hydro One's agents, consultants, contractors and business partners, to the extent feasible. The Code is posted on the corporate intranet site and on the external corporate website at www.HydroOne.com.

Our company has a Corporate Ethics Officer who is accountable for making sure that the appropriate actions are taken to investigate and resolve known or suspected violations of the Code, and for ensuring the tracking and reporting of all violations. The Board monitors compliance with the Code through the Human Resources and Public Policy Committee and the Audit and Finance Committee, to whom the Corporate Ethics Officer reports. The Chief Executive Officer is ultimately responsible for our company's compliance with the Code. Further, the Board of Directors abides by a conflict of interest policy which requires directors to exercise independent judgment when considering transactions and contracts in respect of which a director has a material interest.

In 2008, the Code was updated to reflect changes in Hydro One's organizational structure, corporate accountabilities, and the company's business strategy. The revised Code reflects current best governance and ethics practices, including the introduction of a third-party hotline for the anonymous reporting of any accounting, internal accounting controls or auditing matters. A roll out of the revised Code to employees was completed across the organization.

Board, Committee and Director Assessments and Management's Assessment of the Board

A process is in place for evaluating the effectiveness of the Board and its Committees. The process consists of a long-form and short-form evaluation process. The long-form Board evaluation process consists of three written questionnaires: Board, Individual Director, and Committee Assessments of the Board. The questionnaires are completed bi-annually by each director. The Board Assessment addresses the areas of board responsibility, operation and effectiveness. The Individual Director Assessment allows each director to identify areas for improved individual development and performance. The Committee Assessment addresses areas of committee operations and allows each Committee member to identify areas for improved performance.

In alternate years, a short-form Board evaluation process consisting of a one-page questionnaire in which Board members provide comments on any issues that may be of concern to them, is completed.

In addition to the written questionnaires, the Chair of the Board also meets annually with each director about individual performance and the effectiveness of the Board and Committees.

Management's Assessment of the Board consists of one questionnaire completed annually by members of senior management. This Assessment provides the board with meaningful and constructive feedback on its performance from senior management members.

The responses to each questionnaire are compiled in summary reports, which are reviewed by the Corporate Governance Committee to determine what, if any, actions may need to be taken. The Chair of the Corporate Governance Committee provides a report on the summary reports to the Board.

APPENDIX "A"
AUDIT AND FINANCE COMMITTEE MANDATE

1. Pursuant to By-Law No. 1 of Hydro One Inc. (the "Corporation"), a committee of the directors to be known as the "Audit and Finance Committee" (hereinafter referred to as the "Committee") is hereby established.

2. The Committee shall be composed of a minimum of four directors, and have membership attributes consistent with applicable requirements under the *Securities Act* (Ontario) and regulations there under including:

   - **Independence**. The Committee shall be comprised of directors who shall meet the independence and audit committee composition requirements set forth by applicable securities regulatory authorities, or any governmental or regulatory body exercising authority over the Corporation, as in effect from time to time. A member cannot accept consulting, advisory or compensatory fees, other than compensation for directors' fees and expenses, from the Corporation.

   - **Financial Literacy**. All members are to be financially literate (or shall become financially literate within a reasonable period of time after appointment to the Committee). A member is financially literate if he or she has the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the Corporation's financial statements.

3. The members of the Committee shall be appointed or re-appointed at the Organizational Meeting of the Board of Directors (the "Board") immediately following each annual meeting of the Shareholder of the Corporation. Each member of the Committee shall continue to be a member thereof until his or her successor is appointed, unless such member shall resign or be removed by the Board or shall cease to be a director of the Corporation. Where a vacancy occurs at any time in the membership of the Committee, it may be filled by the Board and shall be filled by the Board if the membership of the Committee is less than four directors as a result of the vacancy. Whenever there is a vacancy on the Committee, the remaining members may exercise all of the powers of the Committee as long as a quorum remains in office.

4. The Board or, in the event of its failure to do so, the members of the Committee, shall appoint a Chair from amongst their number. If the Chair of the Committee is not present at any meeting of the Committee, the Chair of the meeting shall be chosen by the Committee from among the members present. The Committee Chair shall be responsible for the leadership of the Committee, including the preparation of the agenda, presiding over meetings and determining Committee assignments. The Chair presiding at any meeting of the Committee shall have a casting vote in case of deadlock. The Committee shall also appoint a Secretary who need not be a director.

5. The time and place of meetings of the Committee and the procedure at such meetings shall be determined from time to time by the members thereof provided that:

   (a) a quorum for meetings shall be three members, present in person or by telephone or other telecommunication device that permit all persons participating in the meeting to speak and hear each other;

   (b) the Committee shall meet at least quarterly; and

   (c) notice of the time and place of every meeting shall be given in writing by facsimile communication or electronic mail to each member of the Committee, the internal auditors and the external auditors of the Corporation at least 24 hours prior to the time fixed for such meeting, provided, however, that a member may in any manner waive a notice of a meeting; and attendance of a member at a meeting is a waiver of notice of the meeting, except where a member attends a meeting for the express purpose of objecting to the transaction of any business on the grounds that the meeting is not lawfully called. The Committee may request the external auditors to attend a meeting or meetings of the Committee, the expense of which shall be paid by the Corporation and included within the external auditors' annual fee. A meeting of the Committee may be called by the Secretary of the Committee on the direction of the Chair or Chief Executive Officer of the Corporation, by any member of the Committee, the external auditors or internal auditors. Notwithstanding the provisions of this paragraph, the Committee shall at all times have the right to determine who shall and shall not be present at any part of the meeting of the Committee.

6. The Committee Chair is responsible for reporting to the Board on behalf of the Committee on matters considered by the Committee, its activities and compliance with this mandate.

7. For purposes of this Section, the term "Corporation" shall include Hydro One Inc. and its subsidiary entities, as defined by Multilateral Instrument 52-110 Audit Committees.

   The Committee shall:

   (1) in connection with its advisory functions:

      (a) review the internal audit procedures of the Corporation and advise the Board on its auditing practices and procedures and obtain adequate assurance that internal controls are adequate;

      (b) meet separately with the external auditors and internal auditors;

      (c) review the recommendations of the officers of the Corporation as to the reappointment or appointment of external auditors and make recommendations to the Board with respect to the nomination and remuneration of external auditors to be appointed at each annual meeting of the Shareholder. If a change in external auditors is proposed, the

Committee will inquire as to the reasons for the change, including the response of the incumbent auditors, and inquire as to the qualifications of the newly proposed auditors before making its recommendation to the Board;

(d) review periodically, reports on the nature and extent of compliance with requirements regarding statutory deductions and remittances, including deductions and remittances under the *Income Tax Act* (Canada), the *Excise Tax Act* (Canada) and the *Unemployment Insurance Act* (Canada), the nature and extent of non-compliance together with the reasons therefore and the plan and timetable to correct deficiencies and report to the Board on the status of such matters;

(e) review and reassess the Committee's mandate at least annually and report to the Board results of the review, including any recommended changes to the mandate;

(f) the Committee shall meet with management to review and assess the process and systems in place for the review of public disclosure documents that contain audited and unaudited financial information and their effectiveness;

(g) describe in the annual information form all information about the Committee as required by applicable securities regulatory authorities; and

(h) review and assess with management and recommend to the Board for approval any material transaction, contract or other matter involving the Corporation and a shareholder, or other person, which owns directly or indirectly voting securities of the Corporation. For this purpose, "material" means any transaction, contract or matter that significantly affects, or would reasonably be expected to have a significant effect on, the financial position of the Corporation or the market price or value of its securities.

(2) In connection with the exercise of its powers:

(a) review and recommend to the Board for approval:

(i) the audited annual financial statements of the Corporation, the annual management discussion and analysis ("MD&A") and any required annual MD&A supplement and related press releases before the Corporation publicly discloses this information;

(ii) the Corporation's interim (quarterly) financial statements, interim MD&A and any required interim MD&A supplement and related press releases before the Corporation publicly discloses this

information, unless the Board delegates to the Committee such approval authority as provided in paragraph (b) below;

(iii) all financial statements in prospectuses and other offering memoranda, and financial statements required by securities regulatory authorities;

(iv) the annual information form of the Corporation and any other similar disclosure required to be filed by securities regulatory authorities;

(v) any prospectus, offering memorandum of the Corporation, or any amendments thereto. For the purpose of this mandate, reference to "prospectus" includes a preliminary prospectus, a prospectus, or an amendment thereto, but excludes a pricing supplement; and

(vi) the annual financing plans and objectives of the Corporation including, foreign currency risk and interest rate risk strategies.

(b) subject to the authority delegated by the Board, review and approve the Corporation's interim financial statements, interim MD&A and any interim MD&A supplement, and review and approve the related press releases;

(c) discuss with the external auditors results of their review of the interim financial statements and interim MD&A, including any matters external auditors may raise with audit committees under generally accepted accounting principles and auditing standards in compliance with applicable securities laws and regulations;

(d) review the issuance under a shelf prospectus of the Corporation of debentures, notes and/or other unsecured and secured evidences of indebtedness of the Corporation, in accordance with the authority delegated by the Board and the filing with securities regulatory authorities of any prospectus supplement relating thereto;

e) review and oversee the audit plans of the internal auditors and review, pre-approve and directly be responsible for overseeing the work of the external auditors of the Corporation engaged for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services for the Corporation, including the resolution of any disagreements between management and the external auditors regarding financial reporting. The Committee has the authority to communicate directly with the internal and external auditors.

The Committee shall also review the degree of co-ordination between the audit plans of the internal auditors and the external auditors and will inquire as to the extent the planned audit scope can be relied upon to

detect weaknesses in internal control, fraud or other illegal acts. Any significant recommendations made by the auditors for the strengthening of internal controls will be reviewed;

(f) pre-approve all audit and non-audit services to be provided to the Corporation by its external auditors. In connection with non-audit services, the Committee shall adopt specific policies and procedures for the engagement of non-audit services ensuring that the non-audit service is not prohibited or restricted by securities regulatory authorities. The Committee may also delegate to one or more of its members the authority to pre-approve audit and non-audit services, in which event the pre-approval of audit and non-audit services by any such member must be presented to and ratified by the Committee at its first scheduled meeting following such pre-approval;

(g) review the internal control procedures and management's annual internal control report to ensure compliance with the law and avoidance of conflicts of interest including, without limitation, a review of policies and practices concerning officers' expenses and perquisites, including the use of the Corporation's assets;

(h) review the duties and responsibilities of internal audit staff respecting controls, procedures and accounting practices of the Corporation;

(i) review management programs and policies regarding the adequacy and effectiveness of internal controls over the accounting and financial reporting systems within the Corporation and, in particular, the Committee will review management's response to the internal control recommendations of the internal and external auditors;

(j) receive and review regular reports from the internal and external auditors on the appropriateness of the Corporation's significant accounting and disclosure policies and practices and changes thereto, including any areas of management judgment and estimates that have a material effect upon the financial statements, alternative accounting treatments and their ramifications, disagreements between management and the internal and external auditors and include in the review a discussion with the external auditors of the quality, not just acceptability, of accounting principles, the reasonableness of significant judgments, and the clarity and completeness of disclosure;

(k) review with management, the external auditors and, if necessary, with legal counsel, any litigation, claim or other contingency, including tax assessments, that could have a material effect upon the financial position or operating results of the Corporation, and the manner in which these matters have been disclosed in the financial statements;

(l) review, at least annually, the Corporation's corporate insurance program;

(m) annually discuss with external auditors and report to the Board the auditors' independence from management and the Corporation, and in connection, request their written confirmation of independence and disclosure of relationships they have with the Corporation that may be thought to bear on independence, including non-audit related services and fees and their impact;

(n) review the minutes of any audit committee meetings of subsidiary entities of the Corporation and any significant issues and auditor recommendations concerning such subsidiary entities;

(o) review the basis and amount of the external auditor's fees in light of the number and nature of reports issued by the auditors, the quality of the internal controls, the size, complexity and financial condition of the Corporation and the extent of internal audit and other support provided by the Corporation to the external auditors and review all other non-audit fees of the auditors or other accounting firms;

(p) review management's retention of consulting and professional services, including external legal services, on an annual basis;

(q) review and appropriately address any complaints regarding accounting, internal accounting controls, or auditing matters received since the Committee's last meeting, including complaints confidentially submitted by those wishing to remain anonymous; and

(r) receive and review any reports of evidence of a material violation of securities laws or breaches of fiduciary duty tabled by the Corporation's legal counsel as a result of an inappropriate response from management.

(3) review and approve the Corporation's hiring policies regarding partners, employees and former partners and employees of the current and former external auditor of the Corporation.

(4) review, at least on an annual basis:

(a) for information purposes:

(i) the major risks to the Corporation's business objectives;

(ii) overall financing of risk, including the purchase of insurance;

(iii) the risk retention philosophy and risk tolerance guidelines; and

(iv) loss prevention policies and risk management programs;

(b) for approval by the Committee, the Corporation's enterprise risk management policy and framework;

(c) and recommend to the Board for approval all risk management strategies, including foreign currency and interest rate risk strategies.

(5) With respect to the Hydro One Pension Plan and any replacement plan thereof, review the funding policy, the audited annual financial statements, periodic reports detailing the asset mix status and performance of the pension fund and any further pension-related reports or policies to be submitted to the Board, including those resulting from the Terms of Reference of the Pension Committee, the Pension Plan Terms of Reference of the Board of Directors, or the Terms of Reference of the Pension Investments Unit.

8. In instances where members of the Committee believe that in order to properly discharge their fiduciary obligations to the Corporation it is necessary to obtain the advice of independent counsel and other expert advisers, the Committee shall have authority to engage and compensate the appropriate experts. The Board shall be kept apprised of both the selection of the experts and the expert's findings through the Committee's regular reports to the Board.

APPENDIX "B"

HYDRO ONE INC.

BOARD OF DIRECTORS

MANDATE

DUTIES OF THE BOARD OF DIRECTORS

1. The Board of Directors of Hydro One Inc. (the "Board") is responsible for the stewardship of, and has the duty to supervise the management of, the business and affairs of the Corporation including its Subsidiaries, as defined in the *Business Corporations Act* (Ontario).
2. The Board is elected by the sole Shareholder, the Province of Ontario, as represented by the Minister of Energy and Infrastructure (the "Shareholder"). The Board is responsible for seeking and recommending suitable Board candidates to the Shareholder.

ACCOUNTABILITIES AND RESPONSIBILITIES

The Board shall have the accountabilities and responsibilities set out below. In addition, the Board shall perform such duties as may be required under, and act in accordance with the *Business Corporations Act* (Ontario), the Corporation's by-laws, the Memorandum of Agreement with the Shareholder, dated
March 27, 2008 (the "Shareholder Agreement"), as may be amended from time to time, and all applicable laws.

1. **Corporate Governance**
   a. The Board is responsible for developing the Corporation's approach to corporate governance, including developing appropriate policies and procedures and delegating such other matters as it sees fit to the Corporate Governance Committee for its review and consideration.
   b. The Board is responsible for the Corporation's approach to its governance relationship with its sole Shareholder.

2. **Strategic Planning**
   The Board is responsible for:
   a. adopting a strategic planning process and approving, on at least an annual basis, a strategic plan which lays out the strategic direction of the Corporation in the context of the opportunities and risks of the business and the business and commercial environment in which it operates;
   b. reviewing and approving the business, financial, strategic and other plans proposed by management to enable the Corporation to execute its strategy;
   c. adopting processes for monitoring the Corporation's progress toward its strategic and operational goals, and to revising and altering its directions to management in light of changing circumstances affecting the Corporation;

d. taking action when corporate performance falls short of its performance targets or other special circumstances warrant;
e. approving the audited financial statements, interim financial statements and the notes and management's discussion and analysis accompanying such financial statements and the Corporation's Annual Information Form; and
f. reviewing and approving material transactions outside the ordinary course of business, subject to the Shareholder Agreement.

3. **Risk Management**
The Board is responsible for:

a. identifying the principal risks of the Corporation's business and ensuring the implementation of appropriate systems to effectively monitor and manage such risks with a view to the long-term viability of the Corporation;
b. overseeing the integrity of the Corporation's internal control and management information systems;
c. approving, and monitoring compliance with, all significant policies and procedures by which the Corporation is operated; and
d. approving policies and procedures designed to ensure that the Corporation operates at all times within applicable laws and regulations.

4. **Human Resources Management**
a. The Board is responsible for approving the appointment of the President and CEO. The Board is also responsible for approving the compensation of the President and CEO following a review of the recommendations of the Human Resources and Public Policy Committee.
b. The Board will, to the extent feasible, satisfy itself as to the integrity of the President and CEO and other executive officers, and that the President and CEO and other executive officers create a culture of integrity throughout the organization.
c. The Board is responsible for ensuring that succession planning programs are in place, including programs to train, develop, monitor and retain senior management, including the President and CEO.

5. **Communications and Reporting**
a. The Board is responsible for approving and revising from time to time, a disclosure policy to address accurate and timely communications with the Shareholder, bondholders, employees, financial analysts, governments and regulatory authorities, the media and the public.
b. The Board is responsible for overseeing the Corporation's reporting to the Shareholder, responses to requests for information and other reporting obligations as set out in the Shareholder Agreement, and for ensuring open and transparent communication with the Shareholder.

6. **Board Meetings and Materials**

a. The Chair, in consultation with the President and CEO and the General Counsel and Secretary, shall develop the agenda for each Board meeting.
b. Meeting materials shall be provided to directors before each Board meeting in sufficient time to ensure adequate opportunity for review.
c. Independent directors (as defined under applicable securities legislation) shall hold regularly scheduled meetings at which non-independent directors including members of management are not present.

7. **Committees of the Board**
   a. The Board discharges its responsibilities both directly and through its committees: the Audit and Finance Committee, the Corporate Governance Committee, the Human Resources and Public Policy Committee, the Health and Safety Committee and the Regulatory and Environment Committee. In addition to these standing Committees, the Board may from time to time appoint ad hoc Committees to address certain issues of a more short-term nature.
   b. The Board is responsible for approving the mandates for each Board Committee.
   c. To facilitate communication between the Board and each Board Committee, each Committee Chair is responsible for providing a report to the Board on material matters considered by the Committee at the first Board meeting after the Committee's meeting.

DIRECTOR DEVELOPMENT AND EVALUATION

1. Each new director shall participate in Hydro One's Director Education Program and any continuing director development programs.
2. Annually, with the assistance of the Corporate Governance Committee, the Board shall evaluate and review the performance of the Board, each of its Committees, each of the directors and the adequacy of this mandate.